RECOM MANAGED SYSTEMS INC DE/
Form 10KSB
March 31, 2005

**SECURITIES AND EXCHANGE COMMISSION**
**WASHINGTON, D.C. 20549**

**FORM 10 KSB**

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Annual Report Under Section 13 or 15(d) of the Securities Exchange Act of 1934

For the fiscal year ended December 31, 2004

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Transition Report Under Section 13 or 15(d) of the Securities Exchange Act of 1934

For the transition period from ___________ to ___________

Commission file number: ___________

**RECOM MANAGED SYSTEMS, INC.**

(Exact name of small business issuer in its charter)

**Delaware**

(State or other jurisdiction of incorporation or organization)

**87-0441351**

(I.R.S. Employer Identification No.)

**4705 Laurel Canyon Boulevard, Suite 203**
**Studio City, California 91607**
**(818) 432-4560**

(Address of principal executive offices) (Zip code)
(Issuer s telephone number)

Securities registered pursuant to Section 12(b) of the Exchange Act: None

Securities registered pursuant to Section 12(g) of the Exchange Act: None

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 S No £

Check if there is no disclosure of delinquent filers pursuant to Item 405 of Regulation S-B is not contained in this form, and no disclosure will not be contained, to the best of registrant s knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-KSB or any amendment to this Form 10-KSB: S

The issuer s revenues for its most recent fiscal year (fiscal 2004) was $0.

The aggregate market value of the issuer s voting and non-voting common equity held by the issuer s non-affiliates computed by reference to the price at which the common equity was sold, or the average bid and asked price of such common equity, as of a specified date within the past 60 days, was $29,789,000 as of March 25, 2005.

Check whether the issuer has filed all documents and reports required to be filed by Section 12, 13 or 15(d) of the Exchange Act after the distribution of securities under a plan confirmed by a court during the past five years: Yes S No £

The number of shares outstanding of each of the issuer s classes of stock as of as of March 25, 2005, the latest practicable date, was 35,077,947 shares of common stock and 275,323 shares of series A convertible preferred stock.

**Documents Incorporated By Reference**

The issuer has not incorporated by reference into this annual report: (1) any annual report to the issuer s securities holders, (2) any proxy or information statement, or (3) any prospectus filed pursuant to Rule 424(b) or (c) of the Securities Act.

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**ADVISEMENTS**

The information set forth in the section of this annual report captioned *Business* is current as of March 25, 2005, unless an earlier or later date is indicated in that section. The information set forth in the sections of this annual report other than *Business* is current as of December 31, 2004, unless an earlier or later date is indicated in those sections.

On April 11, 2003, we effected a split in our common shares on a 3:1 forward basis through the mechanism of a stock dividend. Whenever we make any reference in this annual report to the grant or issuance of common shares or options or warrants to purchase common shares, such reference shall, for comparison purposes, be made in reference to post-split numbers and, in the case of options and warrants, exercise prices, unless we state otherwise.

In this annual report we make a number of statements, referred to as *forward-looking statements* , which are intended to convey our expectations or predictions regarding the occurrence of possible future events or the existence of trends and factors that may impact our future plans and operating results. These forward-looking statements are derived, in part, from various assumptions and analyses we have made in the context of our current business plan and information currently available to us and in light of our experience and perceptions of historical trends, current conditions and expected future developments and other factors we believe to be appropriate in the circumstances. You can generally identify forward-looking statements through words and phrases such as *seek* , *anticipate* , *believe* , *estimate* , *expect* *intend* , *plan* , *budget* , *project* , *may be* , *may continue* , *may likely result* , and similar expressions. When reac forward looking statement you should remain mindful that actual results or developments may vary substantially from those expected as expressed in or implied by that statement for a number of reasons or factors, such as those relating to: (1) the success of our research and development activities, the development of a viable commercial production model, and the speed with which regulatory authorizations and product launches may be achieved; (2) whether or not a market for our products develops and, if a market develops, the pace at which it develops; (3) our ability to successfully sell our products if a market develops; (4) our ability to attract the qualified personnel to implement our growth strategies, (5) our ability to develop sales, marketing and distribution capabilities; (6) our ability to obtain reimbursement from third party payers for the products that we sell; (7) the accuracy of our estimates and projections; (8) our ability to fund our short-term and long-term financing needs; (9) changes in our business plan and corporate strategies; and (10) other risks and uncertainties discussed in greater detail in the sections of this annual report, including those captioned *Plan of Operation* and *Uncertainties And Risk Factors That May Affect Our Future Results And Financial Condition* .

Each forward-looking statement should be read in context with, and with an understanding of, the various other disclosures concerning our company and our business made elsewhere in this annual report as well as other pubic reports filed with the United States Securities and Exchange Commission (the *SEC* ). You should not place undue reliance on any forward-looking statement as a prediction of actual results or developments. We are not obligated to update or revise any forward-looking statement contained in this annual report to reflect new events or circumstances unless and to the extent required by applicable law.

## BUSINESS

### Overview

Recom Managed Systems, Inc. ( *we* , *our company* or *Recom* ) is a development stage medical device company focused on researching, developing and marketing medical devices which monitor and measure physiological signals in order to detect diseases that impact an individual s health. Physiological signals are small bioelectrical signals generated by the body. Our initial product will be patient modules used as part of a heart monitor system to acquire, amplify and process physiological signals associated with a patient s cardiovascular system. Heart monitor systems are used by heart specialists known as cardiologists to collect physiological data for electrocardiogram or ECG tests for the purpose of detecting and identifying cardiovascular disease. Our patient module will operate using a proprietary and patented amplification technology which provides the capability to enlarge and process the physiological signals to discriminate them from ambient or background electromagnetic noise and to facilitate the examination of the signal data for diagnostic purposes. Our amplification technology is an enhancement of an amplification technology first developed for the United States Air Force to record bioelectrical signals from a pilot s brain, known as an electroencephalogram or EEG. Earlier versions of the technology were also used by the National Institute of Health as well as companies such as Titan Systems and Teledyne, Inc. for purposes of monitoring different physiological signals relating to the brain.

### Corporate History

Recom was originally incorporated in Delaware on January 19, 1987 under the name Mt. Olympus Enterprises Inc.. We had no specific business purpose on the date of incorporation and were inactive until October 30, 1998. On that date, we completed a reverse acquisition with J2 Technologies LLC, a California limited liability company formed on July 31, 1998, which was engaged in the business of developing, servicing and managing commercial computer networks both on-site and remotely. As a consequence of the reverse acquisition, we engaged in J2 Technologies business and changed our name to Recom Managed Systems, Inc. We were subsequently unsuccessful in this business and, on June 26, 2000, filed a voluntary petition for reorganization under Chapter 11 of the Federal Bankruptcy Code. Our plan of reorganization was confirmed by the Bankruptcy Court and the confirmation order became final on November 7, 2000. Subsequent to declaring bankruptcy, we ceased our business operations. The plan of reorganization provided for a total discharge of the company and our officers and directors from all pre-petition debts, expenses and legal causes of action which may have existed on or before the filing of the bankruptcy. The plan further provided for the consolidation of all previously issued common shares, and the issuance of additional common shares to various creditors of the company. As of December 31, 2000, following full implementation of the plan, there were 4,139,784 common shares (1,379,928 shares pre-split) issued and outstanding.

On September 19, 2002, we acquired certain know how, trade secrets and other proprietary intellectual property rights relating to the development of a physiological signal amplification equipment and technology, referred to in this report as the *Signal Technologies* , from ARC Finance Group, LLC, our parent corporation, in exchange for 23,400,000 common shares (7,800,000 shares pre-split). The shares represented approximately 85% of our issued and outstanding common shares. We valued the Signal Technologies at $78,023 for financial accounting purposes, reflecting the ARC Finance Group s cost to acquire the Signal Technologies from Dr. Budimir S. Drakulic as discussed below. The terms of the acquisition were determined by the parties on an arms-length negotiated basis. No independent valuation was sought from a business/technology appraiser or other third party due to financial constraints. There was no relationship between Recom, including our officers, directors and shareholders, and ARC Finance Group, including its officers, directors and shareholders, prior to our acquisition of the Signal Technologies from ARC Finance Group. No finder s fees or other forms of consideration were paid by Recom or ARC Finance Group or our respective officers, directors or shareholders in connection with our acquisition of the Signal Technologies.

The principal component of the Signal Technologies is a patented amplification technology which was originally invented by our Vice President and Chief Technology Officer, Dr. Budimir S. Drakulic. The underlying patent covers methods of discriminating different biomedical signals from ambient electromagnetic noise. Also included in the Signal Technologies was an assignment of a license agreement dated December 9, 1993 between Dr. Drakulic and Teledyne Electronic Technologies pursuant to which Dr. Drakulic granted a limited license to that company to manufacture EEG monitor products based upon an early version of the amplification technology. This license agreement specified that Dr. Drakulic retained ownership of the original patent and underling technology and the right to use technology to develop new products as long as they would not infringe on Teledyne s licensed products. Dr. Drakulic has since received a letter from Teledyne acknowledging that the use of the technology for our proposed heart monitor systems does not infringe on Teledyne s licensed products. Concurrent with our acquisition of the Signal Technologies, we obtained Dr. Drakulic s services as our Vice President and Chief Technology Officer to lead our product development efforts.

ARC Finance Group is a Delaware limited liability company formed in May 2002 which is owned and controlled by Ms. Tracy Hampton. In or about May 2002, ARC Finance Group entered into an understanding with Dr. Drakulic pursuant to which it would fund informal proof-of-concept activities and product development costs to be incurred by Dr. Drakulic in order to establish to the satisfaction of ARC Finance the potential of the Signal Technologies for ECG applications, and would also pay other expenses of Dr. Drakulic, in exchange for the rights to acquire and market the Signal Technologies. Pursuant to that understanding, ARC Finance funded these activities and costs in the amount of $78,023 during the summer of 2002, and acquired the Signal Technologies from Dr. Drakulic when it became satisfied that the Signal Technologies could be applied for ECG applications. Following its acquisition of the Signal Technologies, ARC Finance Group sought a third-party company to license or acquire the Signal Technologies for its commercial development, leading to our acquisition of the Signal Technologies from ARC Finance Group. Since that acquisition, ARC Finance Group has remained a holding company for a passive investment in our company. ARC Finance Group s only investment and business activity to date relates to Recom, ARC Finance Group has no investments other than Recom, sources of revenue or liabilities, and there is no past or current relationship between ARC Finance Group and Titan Systems or Teledyne Inc.

On April 11, 2003, we completed a three for one forward stock split, resulting in a total of 31,510,848 common shares being outstanding as of that date.

We do not consider Recom to be a blank check company as that term is defined in Rule 419 of Regulation C promulgated under the Securities Act of 1933, as amended (the *Securities Act*) as our business plan does not contemplate our engaging in any merger or acquisition with any unidentified company, entity or person. Notwithstanding the foregoing, should we in the future identify a technology, product or business we deem advisable to acquire, we reserve the right to consider that acquisition at that time. We had previously considered the acquisition of a non-prescription heart monitor system from TZ Medical, Inc., however we have decided not to pursue that acquisition.

**Description Of Heart Monitor Systems And ECGs**

A heart monitor system is a system used to monitor and record changes in physiological signals associated with a patient s cardiovascular system. Heart monitor systems are used by heart specialists known as cardiologists to collect physiological data for electrocardiogram or ECG tests for the purpose of detecting and identifying cardiovascular disease. An ECG gives the cardiologist important information about the heart. For example, by examining changes in waveforms from 0.67 Hz to 40 Hz frequency range, a cardiologist can identify irregularities in the heart s rate and rhythm, known as arrhythmia. By examining changes in waveforms in the broader 0.05 Hz to 150 Hz frequency range, a cardiologist can identify different types of heart disease, including damage to the heart muscles or tissue resulting from (1) decreased blood flow attributable to the narrowing of the arteries, known as cardiac ischemia, (2) enlargement of the heart resulting from additional effort attributable to the hardening of the heart muscle, known as hypertrophy, and (3) the existence of past or presently occurring heart attacks.

When an ECG test is ordinarily conducted in a clinical setting, the physiological signals from the patient s heart are displayed through a heart monitor system called a 12-lead ECG, based on acquiring a signal from ten electrodes, one of which is attached to each of the patient s arms, six to the chest and one to each leg. The placement of the ten electrodes enables the heart to be examined for different diseases. Physiological signals generated by the heart are amplified and recorded in the form of a series of waveforms that can be displayed on a screen or printed on paper for interpretation by a cardiologist. Any irregularity in heart rhythm, damage or stress to the heart muscle will result in a deviation from a normal waveform.

There are three settings under which ECGs are normally taken: (1) the clinical or resting setting where the patient is immobile; (2) the ambulatory setting where the patient is mobile; and (3) the exercise setting where the patient is subjected to physical stress in a controlled environment. These three types of ECG tests are more fully described as follows:

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ECGs administered in the resting setting are generally given under either (1) emergency circumstances when an individual complains of symptoms typically associated with heart disease such as chest pains, shortness of breath or heart palpitations, or (2) on an annual basis for older patients as part of their annual physical examination. Most ECGs are obtained in the resting setting. In a resting setting, the principal technical issue in interpreting ECG waveforms arise from the existence of ambient or background noise emanating from other electromagnetic sources, including (1) signals generated by the other organs, muscles and systems of the body, whether from movement or the performance by those organs of their bodily functions, and (2) signals generated by sources external to the body, such as electronic equipment, lights or engines. This ambient noise is commonly referred to as an artifact . As previously discussed, cardiologists can identify irregularities in the heart s rate and rhythm, known as arrhythmia, by examining changes in the 0.67 to 40 Hz frequency range. Because of the relatively large amplitudes of these waveforms in this range, cardiologists can, as a practical matter, easily identify arrhythmia notwithstanding the existence of electromagnetic ambient noise from other sources. However, it is very difficult for cardiologists to distinguish physiological signals from ambient noise in the broader frequency ranges used to identify different types of heart disease, including cardiac ischemia, hypertrophy and the existence of past or presently occurring heart attacks. The reason for this difficulty is that the physiological signals associated with these other heart diseases are of a much lower amplitude or strength in the lower 0.05 to 0.67 Hz and upper 40 to 150 Hz portions of the frequency range, meaning that they do not stand-out from the ambient noise in these portions and therefore cannot be easily discriminated from that ambient noise. In order to minimize ambient noise in the clinical setting, ECGs are normally taken in the hospital or physician offices. Cardiologists instruct the patient to lie in the supine position, being as still as possible while a reading is taken to reduce ambient noise caused by physical movement. Another method to reduce ambient noise is to reduce the sensitivity of the monitoring equipment, although this alternative results in a loss of signal quality and the ability to read certain signal intricacies.

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ECGs administered in the ambulatory setting are given in an attempt to identify heart disease not evident in the resting setting. Heart disease such as cardiac ischemia and cardiac hypertrophy as well as the existence of past or presently occurring heart attacks can escape detection without longer-term monitoring in a physically active or stressful setting. An ambulatory heart monitor system, commonly known as a Holter monitor, allows the patient s heart to be continuously monitored over a period of hours or days, while the patient carries out his or her daily activities under typical conditions of stress away from the physicians office or hospital. The principal technical limitation in deciphering ECG waveforms in an ambulatory setting is that in many cases, ambulatory heart monitor systems are unable to accurately identify many of the heart conditions they are intended to identify due to their inability to clearly distinguish and discriminate the physiological signals associated with these conditions from electromagnetic ambient noise in the lower and upper portions of the full 0.05 to 150 Hz frequency range. Therefore, the industry standard for ambulatory recorders is 0.67 to 40 Hz.

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ECGs administered in the exercise or stress setting are given while the patient exercises on a treadmill, step machine or exercise cycle to enable the cardiologist to monitor, among other things, his heart behavior under



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conditions of physical stress. Exercise can exacerbate cardiovascular abnormalities that are not present at rest and it can be used to determine the adequacy of cardiac function. Similar to an ambulatory ECG, this allows the cardiologist to identify different heart disease such as cardiac ischemia and cardiac hypertrophy as well as the existence of past or presently occurring heart attacks that may not be evident under a clinical resting or simple ambulatory ECG test conditions. However, while external sources of ambient noise can be reduced in the clinical setting when exercise ECGs are conducted, high levels of physical activity inherent in exercise ECGs generate higher internal levels of ambient noise due to necessary patient movement. To address this issue, exercise ECG devices are connected to computers which run sophisticated software to filter and process physiological signals and produce average waveforms for interpretation by the cardiologist. However, the American Heart Association1

and American College of Cardiology2

.each state that computer processing is not completely reliable because of software limitations in handling noise, the technical limitations of the software algorithms and therefore, cardiologists are advised to look at the raw data and not rely solely upon the results obtained by software processing of original data.

**Description of Current Products**

***Model 100 Ambulatory Monitor System***

In December 2004, we completed the design, fabrication and testing of a pre-production model of our first product for commercialization, our battery-operated, digital 12-lead Recom Model 100 Patient Module or *Model 100 Module* . This work was completed for us in December 2004 by Battelle Memorial Institute, Health and Life Sciences pursuant to a research and development services agreement. As discussed below, the Model 100 Module will be used as the primary component of a 12-lead ambulatory heart monitor system to acquire, process, amplify and store physiological signal data. In operation, the Model 100 Module will be used in conjunction with two accessories. The first being a currently-available FDA-cleared or approved electrode/lead wire set which Recom has engineered the Module 100 to be compatible with and recommends for use with the module, and the second being a currently-available personal digital assistant or PDA device which Recom has also engineered the Module 100 to be compatible with and will recommend for use with the module. Once physiological data is recorded and stored, it will then be interpreted at a later date by a cardiologist using currently-available FDA-cleared or approved ECG analysis software program. By way of example, Recom currently intends to design the Model 100 Module to work with FDA-cleared and available electrodes and lead wire sets such as the ConMED D-series ECG Cable and 3M Red Dot Snap Monitoring Electrodes, and for its data to be interpreted by FDA-cleared analysis software programs marketed such as those offered by Northeastern Monitoring, Mortara, Phillips and/or General Electric. In this report and, as discussed below, in Recom s regulatory filings with the FDA, we refer to the foregoing heart monitor system by which the Model 100 Module interfaces with compatible FDA-cleared or approved electrode/lead wire sets and PDAs as the *Model 100 Monitor System* , and the compatible electrode/lead wire sets, PDAs and ECG analysis software as the *ancillary products* .

The Model 100 Monitor System is an ambulatory patient heart monitor or recording system that will allow a patient s heart to be continuously monitored over a period of 24 to 48 hours while the patient carries out his or her daily activities away from the physicians office or hospital. As previously noted, the primary component of the monitor system is the Model 100 Module, a compact device approximately 4 x 3.5 x 1.5 inches in size and 5.5 oz. in weight, which acquires the physiological signals from the patient by means of the electrodes; processes and amplifies the signals using the Signal Technologies; and then transmits the signal data wirelessly to the PDA to be stored as a file on a flash card. Patients using the Model 100 Monitor System will be able to move around freely while data is collected by patient module and sent in real time from the patient module to the PDA and stored on the flash card. At the conclusion of the recording period, the patient returns the Model 100 Monitor System to the cardiologist, who

1

ACC/AHA 2002 Guideline Update for Exercise Testing, Gibbons RJ et al.

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Exercise Standards for Testing and Training: S Statement for Healthcare Professionals, Fletcher GF et al, Circulation 104:1694-1740, published on October 2, 2001.



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retrieves the flash card and places it in a reading analysis station on which an ECG analysis software program is installed. The raw ECG recorded data is then analyzed by the software providing the cardiologist with the results for interpretation. The Model 100 Monitor System is a non-diagnostic system insofar as it records, processes and stores physiological signals, but does not contain diagnostic software for signal interpretation.

The Model 100 Module can be used with any FDA-cleared or approved electrode/lead wire set or PDA, and the signal data produced by the Model 100 Monitor System can be interpreted by any FDA-cleared or approved ECG analysis software, so long as we have listed that equipment or software as being compatible with the module or signal data produced by the monitor system in our packaging in accordance with FDA labeling regulations. For example, the Model 100 Module can be connected to a patient via commercially available cable and electrodes as discussed above. As a practical matter, the determination and provision of the electrode/lead wire set and PDA to be used with the Model 100 Module will be made by patient s cardiologist and the cardiologist will also use his software program to manage and interpret the data in making his diagnosis. We are currently identifying one or more ancillary products that we would recommend for use with the Model 100 Module as part of the monitor system. Upon our identification of the ancillary products with which the Model 100 Module can be operated, we will modify the module to ensure computability.

Our Model 100 Monitor System is a Class II medical device that must be cleared by the FDA in order to be marketed within the United States. On January 28, 2004, we received FDA 510(k) clearance under the FDA s abbreviated 510(k) submission format allowing us to market our Model 100 Monitor System, i.e., our Model 100 Module used in conjunction with its FDA-cleared or approved ancillary products, on the basis of it being substantially equivalent to other ambulatory monitor systems on the market which satisfy the industry s consensual ANSI/AAMI EC-38 standard for non-diagnostic monitor systems. Under the terms of the abbreviated 510(k) clearance, we are required to have supporting data in our files documenting that our Model 100 Monitor System will conform to performance standards before marketing the Module 100 Module. As such, we may continue to perform engineering and design work on the Model 100 Module without resubmitting the system for further FDA 510(k) clearance unless we were to significantly alter the safety or effectives of the system as cleared by FDA. We do not anticipate this will occur.

As previously noted, we engaged Battelle Memorial Institute, Health and Life Sciences to design, fabricate and test the pre-production model of our Model 100 Module pursuant to a research and development services agreement completed by Battelle Memorial Institute in December 2004. Battelle Memorial Institute is a global science and technology enterprise with over 16,000 scientists, engineers and support staff that develops and commercializes technology and manages laboratories for customers. The pre-production model of our Model 100 Module was tested and determined to comply with all applicable performance, safety, environmental and regulatory standards, including the FDA-recognized consensual ANSI/AAMI EC-38 industry standards for ambulatory ECG devices, Federal Communications Commission ( FCC ) requirements for Human Exposure to Radiofrequency (RF), the FDA-recognized consensual industry standards for electromagnetic compatibility for medical devices (EMC), the FDA-recognized IE 60601-1 international safety standard relating to medical electrical equipment, and the FDA's Quality System Regulations. These testing results also satisfied our obligation under our abbreviated 510(k) submission to have supporting data in our files before marketing the Model 100 Module as part of the Model 100 Monitor System. As part of our contract with Battelle Memorial Institute, it also manufactured 24 pre-production patient modules which we will use for user preference testing with physicians, hospitals and clinics as discussed below. We anticipate that we will introduce our Model 100 Monitor System to the market at the American College of Cardiolology Convention to be held in March 2005, and will start selling the devices in early 2006. In anticipation of formal product introduction, we must make a final determination as to the FDA-approved ECG analysis software system that we will recommend that cardiologists use with our Model 100 Monitor System, and finalize third-party contract manufacturing arrangements.

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**Description of Products Or Services In Investigatory or Early Research & Development Stage**

***Diagnostic Ambulatory Monitor System***

As previously noted, our Model 100 Module will acquire physiological signals from a patient and store the signal data file on a flash card, which will be delivered to the cardiologist for download and analysis. In the longer term we intend to investigate the development of an enhanced version of our Model 100 Module with ANSI/AAMI EC-11 and EC-13 diagnostic ECG features and alarm functions integrated into the patient module (the *Model 200 Module*) that would continuously transmit data wirelessly over the Internet to a patient monitoring center as discussed below. A diagnostic heart monitor is one which can instantaneously interpret data and identify heart conditions, such as arrhythmia. The Model 200 Module would allow the physician to access the patient record at any time for analysis by simply logging into the server over the Internet, thereby avoiding the necessity of delivering a flash card as contemplated with the Model 100 Module. In cases of the occurrence of a life-threatening cardiac event, the Model 200 Monitor System would then also transmit a warning or alarm to the patient monitoring center that would be immediately conveyed to the cardiologist for appropriate action. Similar to the Model 100 Module, the Model 200 Module would be used with commercially available FDA-cleared electrodes and diagnostic software. In this report, we refer to the Model 200 Module and its ancillary products and services as the *Model 200 Monitor System*.

On March 3, 2005, we entered into a research and development services agreement with Battelle Memorial Institute to design, fabricate and test a pre-production model of the Model 200 Module. As previously noted, Battelle previously completed the design, fabrication and testing of our Model 100 Module in December 2004. Under the agreement, Battelle will perform its services over a period of 16 months for a fee of $2,815,000, payable as services are performed. This agreement is terminable by either party upon the provision of 30 days notice.

There are several significant hurdles we would need to satisfactorily address in order to develop the Model 200 Module, including our ability to develop of the software necessary to process and forward the signal data to a patient monitoring center, and to establish compliance with the ANSI/AAMI EC-11 and EC-13 standards for diagnostic ECG systems. The Model 200 Monitor System would also require FDA approval. We can give you no assurance that we will be successful in developing the Model 200 Monitor System including developing the necessary software, procuring the necessary FDA approval or clearance for these products and services, or competitively marketing these products and services.

***Patient Monitoring Center***

As just discussed, the Model 200 Monitor System would transmit signal data and alarms to a patient monitoring center for access over the Internet by a cardiologist. Several companies currently offer monitoring services for heart monitor products using a variety of transmission methods, such as the telephone and the Internet, so the use of a patient monitoring system with the Model 200 Monitor System would not be considered to be novel. The establishment of a patient monitoring center enable us to receive a continuous stream of revenues from modules we sell, which would allow us to substantially enhance our revenues over the initial sale of those modules. Should we proceed with this project, we would most likely either develop our own monitoring centers or acquire an ongoing monitoring business, although we might also consider licensing our software to independent monitoring centers. As part of this project we are also investigating the development of continuous preventative monitoring software that could be used by the cardiologist to analyze collected signal data continuously collected through the monitoring process.

Before making any decision relating to the establishment or acquisition of a patient monitoring center and continuous monitoring software project, there are numerous business and technical issues we would need to resolve. Further, the patient monitoring centers and software would also require FDA approval, and the server and network at the patient monitoring center would also need to be compliant with the Health Insurance Portability and Accountability Act, which requires that we meet federally mandated requirements when handling patient data.

At this point we remain in the early investigation stage relative to establishment or acquisition of patient monitoring centers and continuous monitoring software, and cannot provide any guidance as to any estimated timeframes as to when or even if we would formally commence or complete the project, or as to any of the estimated costs involved. Should we proceed with the project, we can give you no assurance that we will be successful in establishing or acquiring the patient monitoring centers, procuring the necessary FDA approval or clearance for these services, or competitively marketing these services.

***Patient Vest And Electrodes***

We are also in the early stages of investigating the development of a patient vest containing electrodes to be used with our ambulatory heart monitor systems as an alternative to the currently-available FDA-cleared or approved electrode/wire sets. We believe that a patient vest may provide a better signal in an ambulatory setting than the current use of electrodes since the vest as conceived would ensure that the electrodes remained affixed to the body in the correct location throughout the monitoring period. We also believe that the vest will be more convenient and comfortable for a patient. The design is planned to allow a patient to use the vest on a 24/7 basis for extended periods of time, being removed only intermittently for showers, etc. We must address two engineering issues in developing this vest. First, we need to develop an electrode which can be incorporated into the vest to monitor the patient s heart signal, thus replacing the use of leads and gels currently used in recording ECGs. Second, we need to design the vest in such a fashion that it not only holds the electrode against the body at the correct locations and in the proper manner, but it also can be adapted to fit patients with different heights, weights and physiques. At this point we have not ascertained whether we will be able to develop a workable vest that is not too bulky or otherwise impracticable to wear. We are also in the early stages of investigating the development of an improved electrode to be used with our system. Both the ECG patient vest and new ECG electrodes as presently conceptualized will require FDA approval or clearance. We have not to date determined the cost or timeframe to procure FDA approval or clearance.

We can give you no assurance that we will be successful in developing the patient vest or enhanced electrodes at all or within the timeframes or at the costs estimated, or in procuring FDA approval or clearance for these products, or in designing and engineering durable, reliable and competitively priced production versions of any of these products.

**Description of Signal Technologies**

Our patient modules will operate using the Signal Technologies. The Signal Technologies are a patented amplification technology originally developed by our Vice President and Chief Technology Officer, Dr. Budimir S. Drakulic, to address the electrical interference or noise issue. In an effort to explore ways to accurately and objectively monitor pilot performance, the United States Air Force desired to record a pilot s neurological brain responses, consisting of tiny electrical impulses generated by the brain, to different tasks and stresses that occur in-flight using an electroencephalogram or EEG test. However, the Air Force found that the neurological signal monitoring equipment then available was not able to accurately monitor EEG in an electromagnetically-charged environment such as the cockpit of a fighter jet or a B-52 bomber. In 1992, Dr. Drakulic led a team from UCLA and the Veterans Administration in an effort to develop a device to resolve this problem. This effort resulted in the creation by Dr. Drakulic in 1994 of a first-generation amplifier that was successfully used by the Air Force to monitor pilot EEG signals. This early version amplifier is also currently used by the National Institute of Health as well as companies such as Titan Systems and Teledyne, Inc. for purposes of monitoring different physiological signals.

The Signal Technologies were originally acquired by ARC Finance Group from Dr. Drakulic and then by Recom from ARC Finance Group, based upon the belief of Dr. Drakulic and the principals of these companies that the capability of the technology to discriminate EEG signals, particularly in an electromagnetically-charged environment such as fighter aircraft cockpits, would have a similar application in discriminating ECG signals from ambient noise. Specifically, it was and continues to be believed by these persons that the Signal Technologies; as applied to the ECG market, would have the ability to amplify and discriminate the lower-amplitude electromagnetic physiological signals associated with those in the lower and upper portions of the full 0.05 to 150 Hz frequency

range, thereby facilitating the ability to more clearly identify heart diseases in an ambulatory setting. In developing Recom s initial ambulatory patient modules and overall heart monitor systems, and adopting the Signal Technologies for those modules and systems, Dr. Drakulic has since enhanced the signal processing technology such that Recom has filed three additional patents covering these enhancements. In order to validate our beliefs as to the performance of our technology in the ECG market, on August 30, 2004 we entered into an agreement with the Duke Clinical Research Institute at Duke University to evaluate the performance of our Model 100 Monitor System against top-end ECG systems. Under this agreement, the Duke Clinical Research Institute will evaluate our Model 100 Monitor System for 50 to 90 patients. We anticipate that the study will be completed in August 2005, and published in November 2005. Since commercial models of our Model 100 Monitor System have not yet been fully tested as to their performance characteristics against top-end non-diagnostic ECG systems, no assurance can be given that the Signal Technologies will perform as anticipated in either the non-diagnostic or diagnostic ECG settings.

**EEG Products**

We have initiated a study of the applicability of our technology to electroencephalogram or EEG-related applications, in particular the detection of Alzheimer s, Parkinson s and other neurological diseases. As previously discussed above, earlier versions of our amplification technology are now used in EEG equipment used to measure neurological or brain responses. We believe the enhancements Dr. Drakulic has designed since for ECG purposes may have similar application for the EEG market. As discussed below in this report, this activity will not impact the Teledyne licensing agreement. We believe that we will have sufficient initial data by mid-2006 to determine whether or not to proceed to full development of an EEG monitor device.

**Competition**

Our principal competitors in the ambulatory heart monitor market include CardioNet, Inc., which markets a 3-lead, ambulatory ECG monitor system claimed to record and wirelessly transmit physiological data by radiofrequency (RF) to a handheld PDA for subsequent modem or Internet transmission; Cardiac Telecom, Inc., which markets an ambulatory heart monitor system claimed to wirelessly transmit ECG data by way of a processor/phone-connected station; Raytel Medical, which markets an ambulatory heart monitor system claimed to transmit data by telephone; Mortara Instrument, which manufacturers and markets a 12-lead Holter ECG system; and Card Guard, which markets event recorders as well as operating monitoring centers through its two divisions in the United States, Instromedix and Lifewatch.

The market for heart monitoring products and services is intensely competitive and characterized by rapidly changing technology, evolving industry standards, and price competition. There are no substantial barriers to entry, and we expect that competition will be intense and may increase. Many of our existing competitors may have substantially greater financial, product development, technical and marketing resources, larger customer bases, longer operating histories, better name recognition and more established relationships in the industry. As a result, certain of these competitors may be able to develop and expand their product and service offerings more rapidly, adapt to new or emerging technologies and changes in customer requirements more quickly, take advantage of acquisition and other opportunities more readily, devote greater resources to the marketing and sale of their products and services, or aggressively reduce their sales prices below the our costs. We cannot assure you that we will be able compete successfully with existing competitors or new competitors.

**Market Size**

Cardiovascular disease is the leading cause of death in the industrialized world. According to the American Heart Association s *Heart Disease and Stroke Statistics 2004 Update* :

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Heart disease and stroke, the principal components of cardiovascular disease, claim more lives in the United States each year than the next five leading causes of death combined;



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Approximately 61,800,000 people in the United States suffer from one or more types of cardiovascular disease each year;

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Approximately 950,000 lives were claimed by cardiovascular diseases in the United States in 1999;

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Patients who have suffered heart attacks in the United States number 7.3 million, congestive heart failure 4.7 million, arrhythmia 2.0 million, and angina 6.4 million;

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Approximately one-sixth of all people in the United States killed by cardiovascular disease are under the age of 65; and

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In 2004 the estimated direct and indirect healthcare cost of cardiovascular disease in the United States will be $368.4 billion.

The Center for Disease Control has stated that, if all forms of major cardiovascular disease were eliminated, life expectancy would rise by almost seven years while, in comparison, if all forms of cancer were eliminated, the gain in life expectancy would only be three years.

Based upon the foregoing statistics, we believe that patients with any of these health problems would most likely, benefit from Recom s heart monitoring technology and systems.

**Marketing And Distribution Strategy**

Our current plans are to market and distribute our ambulatory patient modules under our own label. We anticipate that we will delegate most sales, marketing and distribution activities for our patient modules to third party, medical-device marketing and distribution companies on a regional basis, while creating a small internal sales, marketing and distribution management staff to oversee these activities and to explore joint venture relationships. In the case of the resting and exercise heart monitoring systems we anticipate developing at some future date, we anticipate licensing our patient module designs and technologies to established medical device manufacturers and distributors, who will most likely, incorporate them into their own systems.

**Manufacturing Capacity**

To date we have fabricated our prototypes and proof of concept devices in-house and with engineering consultants such at Battelle Memorial Institute. Our manufacturing strategy dictates that we will rely upon third party FDA-certified contract manufacturers or joint-venture partners both domestically and off-shore to satisfy production requirements when we are able to introduce our products to market. Most of the components of our products are standard parts which will be available from multiple supply sources at competitive prices. This, coupled with the significant start-up cost advantages associated with contractors, particularly off-shore contractors, should minimize production and product costs.

**Research And Development**

We currently conduct research and early stage development activities in-house and with engineering consultants. We retain title to all improvements or enhancements to our technology developed by or worked on by our engineering consultants under their contracts. Our research and development expenses for fiscal 2004 and 2003 were $1,663,362 and $497,631, respectively. None of these expenditures were borne by customers. We have budgeted $3,000,000 for research and development for fiscal 2005.

**Regulatory Overview**

***FDA Regulations And Requirements***

ECG heart monitor products are regulated in the United States by the Food and Drug Administration (the *FDA* ) under the Medical Device Amendments of 1976 (the *Medical Device Act* ), a section of the Federal Food, Drug & Cosmetic Act (the *FDC Act* ). Under the Medical Device Act, medical devices are designated as Class I, II or III devices depending upon the level of control and review necessary to assure the safety and effectiveness of the device, which in turn is based upon the level of risk to the patient. ECG heart monitor products are classified as a Class II medical device, which cannot be sold in the United States unless the seller can first demonstrate or represent to the FDA pursuant to section 510(k) of the FDC Act, that the device is substantially equivalent to one or more similar devices currently on the U.S. market, referred to as predicate devices. To demonstrate substantial equivalency, the applicant must show that the new device (1) has the same intended use as the predicate device or devices; and (2), has either the same technological characteristics as the predicate device or devices, or has different technological characteristics that do not raise new questions of safety and effectiveness. A claim of substantial equivalence does not mean the new and predicate devices must be identical. Substantial equivalence is established with respect to intended use, design, energy used or delivered, materials, performance, safety, effectiveness, labeling, biocompatibility, standards and other applicable characteristics. Until the applicant receives clearance declaring a device substantially equivalent, it may not proceed to market the device within the United States.

The review period and FDA determination of substantial equivalence should be made within 90 days of submission of a 510(k) application, unless additional information or clarification or clinical studies are requested or required by the FDA. As a practical matter, the review process and FDA determination can take significantly longer than 90 days.

It should be noted that 510(k) clearance is a grandfather process. As such, 510(k) clearance does not imply that the safety, reliability and effectiveness of the medical device has been approved or validated by the FDA, but merely means that the medical device is determined to be substantially equivalent to a previously cleared commercially-related medical device.

As an alternative to the traditional 510(k) submission process, the FDA has also adopted an abbreviated or summary 510(k) submission process in cases where device-specific guidance documents or special controls have been established, or the FDA has recognized a relevant consensus standard, and the applicant certifies compliance or conformance with those documents, controls or standards. The applicant can procure abbreviated 510(k) clearance by either; (1) submitting a declaration that the applicant has in its files test data confirming that the medical device conforms to the consensus standard at the time of submission; or (2) submitting a statement that the medical device will conform to the consensus standard and that the applicant will have that supporting data in its files before marketing the device. Under either approach, the FDA reviewers will normally accept the declaration or statement without requesting the submission of information demonstrating conformity with the standard. In the case of ECG heart monitor products, the FDA has recognized the EC-38 Ambulatory Electrocardiograph, EC-11 Diagnostic ECG, and EC-13 Arrhythmia Detection and Alarm standards adopted by the American National Standards Institute or ANSI and the Association for the Advancement of Medical Instrumentation or AAMI as voluntary consensus standards for Class II 510(k) submission purposes.

Both domestic and foreign manufacturers and distributors of medical devices that intend to market those devices in the United States must register their establishments with the FDA and annually update the registration. Registration provides the FDA with the location of medical device manufacturing facilities and importers. In addition, all medical devices that are manufactured and imported into the United States must be listed with the FDA. Medical device listing is a means of keeping the FDA advised of the generic categories of devices an establishment is manufacturing and marketing.

Manufacturing facilities must undergo FDA inspections to assure compliance with good manufacturing practices or GMPs set forth under the quality system or QS regulation promulgated by the FDA. The quality system regulation provides a basic framework to ensure that manufacturers of finished medical devices intended for commercial distribution in the United States have in place a quality system for the design, manufacture, packaging, labeling, storage, installation and services of finished medical devices intended for commercial distribution in the United States. These regulations require that various specifications and controls be established for devices; that devices be designed under a quality system to meet these specifications; that devices be manufactured under a quality system; that finished devices meet these specifications; that devices be correctly installed, checked and serviced; that quality data be analyzed to identify and correct quality problems and that complaints be processed. Thus, the quality system regulation helps assure that medical devices are safe and effective for their intended use. The FDA monitors device problem data and inspects the operations and records of device developers and manufactures to determine compliance with the GMPs.

Medical devices sold in the United States must also conform to general labeling requirements adopted by the FDA stipulating the content and format of product information that must be provided with the device, including information relating to the manufacturer of, and the intended use of the device, as well as directions for use of the device.

Under Medical Device Reporting or MDR regulations established by the FDA, manufacturers, distributors and users of medical devices are required to report complaints of device malfunctions or incidents of serious injuries or deaths associated with medical devices to the FDA. The MDR regulations provide a post-surveillance mechanism for the FDA and manufacturers to identify, monitor and track significant adverse events involving medical devices for the purpose of detecting and correcting problems in a timely manner.

The FDA has established regulations governing the voluntary recall of medical devices by a manufacturer or importer should it be determined that the devices are defective, present a risk of injury, or are deceptive. Under the Medical Device Recall Authority regulation promulgated by the FDA, that agency also has the authority to order the involuntary recall of medical devices. Under the Medical Device Corrections And Removal regulations established by the FDA, manufacturers and importers are required to report to the FDA the occurrence of any correction or removal of a medical device where made to reduce a risk to health or a violation of the FDC Act.

The FDA has established regulations governing the import and export of medical devices. For a Class II medical device to be legally imported into the United States, it must meet FDA regulatory requirements. At this time, the FDA does not recognize regulatory approvals from other countries. Any Class II medical device may be legally exported from the United States without prior FDA notification or approval so long as it is in legal commercial distribution within the United States. Legal commercial distribution means that (1), the manufacturing establishment is registered with the FDA; (2) the device is listed with the FDA; (3) the sale of the device in the United States is authorized by either 510(k) notification or pre-market approval (PMA); (4) FDA labeling requirements are satisfied; and (5) the device is manufactured in accordance with GMP practices stipulated under the QS regulation. While the FDA does not place any restrictions on the export of these medical devices, certain countries may require written certification that a manufacturer or its devices are in compliance with U.S. law. In such instances the FDA will accommodate the exporter by providing a certificate of compliance called a Certificate for Foreign Government or CFG . If the medical device does not satisfying the foregoing requirements, it may be generally exported under two alternatives. First, if 510(k) clearance for the device is pending in the United States, it may be exported upon a showing that the device will reasonably obtain 510(k) clearance. In addition, the exporter must obtain a Certificate of Exportability from the FDA should the foreign country or consignee request assurance that the device complies with U.S. law. If the exporter does not intend to market the device in the United States, he may obtain a Certificate of Exportability to export the device based upon a showing that the device (1) complies with the laws of the foreign country; (2) meets the foreign purchaser s specifications; (3) is labeled for export on the shipping carton; and (4) is not sold or offered for sale in domestic commerce.

The failure of the manufacturer, importer, distributor or user to meet any of the FDA requirements imposed on it under the FDC Act or administrative regulations adopted thereunder by the FDA, may subject it to civil money penalties, administrative remedies or legal remedies under that Act or regulations.

***Other Regulations And Requirements***

Our heart monitor products and systems must also conform to a number of performance, safety, environmental and regulatory standards, such as those relating to electromagnetic interference, electromagnetic susceptibility, shock and current leakage, and transmission frequency. These standards include the IEC60601-2-27 requirements for the safety of electrocardiograph devices; the IEC 60601-1-2 requirements for safety and electromagnetic compatibility; the UL2601-1 medical equipment general requirements for safety, and FCC regulations under part 15, subpart C, governing allowable frequency ranges for different types of transmission devices, including medical devices.

The server and network we will use in our monitoring station to collect heart data must comply with the Health Insurance Portability and Accountability Act, which requires that we meet federally mandated requirements when handling patient data.

**Patents And Licenses**

We hold patent number 5,678,559 issued by the United States Patent and Trademark Office for our core technology, the Recom amplification device. This patent, labeled *A Method and System of Recording Different Physiological Signal from a Human Body* , describes methods of discriminating different biomedical signals from ambient electromagnetic noise. This patent, which was assigned to us by ARC Finance Group as part of our acquisition of the Signal Technologies, was granted on October 21, 1997 and expires on October 21, 2014.

We also hold the following patent applications filed with the United States Patent and Trademark Office:

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number 10/293,105 captioned *System for, and Method of, Acquiring Physiological Signals of a Patient* filed on November 13, 2002, which describes technical methods for processing and amplifying physiological signals;

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number 10/611,696 captioned *Amplified System for Determining Parameters of a Patient* filed July 1, 2003; which describes methods of amplifying physiological signals while a patient is ambulatory without changing the characteristics of the signal;

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number 10/664,711 captioned *Apparatus for, and Method of, Determining the Characteristics of a Patient s Heart* filed September 17, 2003, which describes the use of electrodes and amplifiers in a vest;

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a patent for which a number has yet to be assigned captioned *System for, And Method of, Monitoring Heartbeats of a Patient,* filed on December 9, 2004, which describes technical methods for monitoring a patient s heart; and

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a patent for which a number has yet to be assigned captioned *Electrode for and Method of, Indicating Signal Characteristics at Particular Positions in a Patient Body* filed on December 9, 2004, which describes electrodes for monitoring a patient s heart.

Dr. Drakulic is the inventor named in our core patent and in each of the above patent applications. We are currently waiting for initial comment from the United States Patent and Trademark Office on each of the above patent applications, which generally occurs between two and two and one-half years after submission based upon current Patent and Trademark Office staffing levels. We anticipate that it will take three to four years for the above patent applications to issue**.**

Also included in the Signal Technologies agreement was an assignment of a license agreement dated December 9, 1993 between Dr. Drakulic and Teledyne Electronic Technologies pursuant to which Dr. Drakulic granted Teledyne a limited license to manufacture and sell EEG monitor products based upon early version of the amplification technology. We do not expect to earn significant revenues from that license. To our knowledge Teledyne is not currently marketing any EEG devices using that early version of the amplification technology, and we do not anticipate that they will in the future market any such products due to technical advancements that they would be required to incorporate into the products. We believe that the incorporation of these advancements would effectively change the underlying product from that which was licensed. Based upon the foregoing, we do not believe the license will prevent Recom from competing in the broader market for EEG diagnostic products.

**Competition**

Because we do not yet have a saleable product, we have no competitive presence in the medical monitoring device market. When our heart monitor system is available for sale, we do not expect to establish a competitive presence in this market for several years, if at all. There are numerous suppliers of heart monitor products, all of which have established products and methods of distribution as well as more money. We may never be able to compete successfully in this or any other medical device market.

**Costs And Effects Of Compliance With Environmental Laws**

There are no special or unusual environmental laws or regulations that will require us to make material expenditures or that can be expected to materially impact on the operation of our business.

**Subsidiaries**

On October 21, 2003, we formed Memonitor, Inc., a Delaware corporation, to act as a vehicle for the prospective application of our technology for the treatment and monitoring of Alzheimer s, Parkinson s and related neurological diseases of the brain. To date, Memonitor has not commenced business activities, and we will not activate this subsidiary until further developments relating to our pending studies of EEG applications for our technology.

**Employees**

We currently have eight full-time employees and engage the services of seven engineering, marketing and financial consultants on a part-time basis. None of our employees is represented by a labor union and we consider our relationships with our employees to be good.

## PROPERTIES

Our executive offices are located at 4705 Laurel Canyon Boulevard, Suite 203, Studio City, California. We lease these facilities, consisting of approximately 3,550 square feet and encompassing four suites including our administrative offices and research and development/laboratory facilities, from Bershin Properties I, LLC through August 31, 2005. We may terminate the lease upon 30 days notice and the payment of two months rent. We currently pay approximately $8,600 per month in base rent for these facilities, which we believe reflects market value, and are also required to pay our share of any increase in operating expenses after August 2002. Operating expenses include expenses for maintenance of common areas, heating, air conditioning, plumbing, trash disposal, janitorial and security services and other like expenses. The leased premises are in good condition and we believe they will be suitable for our purposes for at least twelve months. There is no affiliation between Recom or any our principals or agents and Bershin Properties I, LLC or any of its principals or agents.

**FINANCIAL STATEMENTS AND SUMMARY FINANCIAL DATA**

Our financial statements and notes thereto are filed in a separate section at the end of this annual report. The following tables summarize the consolidated statements of operations and balance sheet data for our company for the periods or as of the dates indicated, respectively:

| | Year Ended December 31, | |
|---|---|---|
| | **2004** | **2003** |
| **Consolidated Statements of Operations Data:** | | |
| Revenue | $ | $ |
| Research and development expenses | $ (1,663,362) | $ (497,631) |
| General and administrative expenses | $ (5,052,580) | $ (4,818,443) |
| Other income (expense) | $ (250,301) | $ 4,697 |
| Net loss | $ (6,966,243) | $ (5,311,377) |
| Preferred dividend | | |

| | | |
|---|---|---|
| | $ | (295,452) |
| | $ | (1,953,170) |
| Net loss attributable to common stockholders | | |
| | $ | (7,261,695) |
| | $ | (7,264,547) |
| Basic and diluted loss per share | | |
| | $ | (0.21) |
| | $ | (0.17) |
| Basic and diluted loss per share attributable to common stockholders | | |
| | $ | (0.22) |
| | $ | (0.23) |
| Weighted average shares outstanding, basic and diluted | | |
| | | 33,632,117 |
| | | 31,765,404 |

| | |
|---|---|
| | **December 31, 2004** |
| **Consolidated Balance Sheet Data:** | |
| Current assets | |
| | $ 2,577,712 |
| Total assets | |
| | $ 3,052,000 |
| Current liabilities | |

| | |
|---|---|
| | $ 2,096,399 |
| Total liabilities | |
| | $ 2,096,399 |
| Total stockholders equity | |
| | $ 955,601 |
| Total liabilities and stockholders equity | |
| | $ 3,052,000 |

**PLAN OF OPERATION**

**General**

The following discussion of our financial condition and results of operations should be read in conjunction with our audited financial statements for the year ended December 31, 2004 and explanatory notes included as part of this report.

**Overview**

Recom is a medical device company focused on researching, developing and marketing medical devices which monitor and measure physiological signals in order to detect diseases that impact an individual s health. Physiological signals are small bioelectrical signals generated by the body. Our initial product will be patient modules used as part of a heart monitor system to acquire, amplify and process physiological signals associated with a patient s cardiovascular system. Heart monitor systems are used by heart specialists known as cardiologists to collect physiological data for electrocardiogram or ECG tests for the purpose of detecting and identifying cardiovascular disease. Our patient module will operate using a proprietary and patented amplification technology which provides the capability to enlarge and process the physiological signals to discriminate them from ambient or background electromagnetic noise and to facilitate the examination of the signal data for diagnostic purposes. Our amplification technology is an enhancement of an amplification technology first developed for the United States Air

Force to record bioelectrical signals from a pilot s brain, known as an electroencephalogram or EEG. Earlier versions of the technology were also used by the National Institute of Health as well as companies such as Titan Systems and Teledyne, Inc. for purposes of monitoring different physiological signals relating to the brain.

In December 2004, we completed development of a pre-production model of our first product for commercialization, our battery-operated, digital 12-lead Recom Model 100 Patient Module or *Model 100 Module* . The Model 100 Module will be used as the primary component of a 12-lead ambulatory heart monitor system, referred to as the *Model 100 Monitor System* . The Model 100 Monitor System is an ambulatory patient heart monitor or recording system that will allow a patient s heart to be continuously monitored over a period of 24 to 48 hours while the patient carries out his or her daily activities away from the physicians office or hospital. The pre-production version satisfies all performance, safety, environmental and regulatory standards. We are now in the process of conducting various user preference performance comparison tests relative to top-end ECG systems in anticipation of our planned introduction of the Model 100 Monitor System to market. We do not anticipate that we will introduce our Model 100 Monitor System to the market until March 2005, and will not start selling the device until early 2006.

**Development Stage Company; Going Concern**

We are a development stage company under the provisions of SFAS No. 7, and have negative cash flows from operations and no current established source of revenue. At present, we only have sufficient capital on hand to fund our operations only through August 2005 (assuming we reduce our expenditures to minimal levels and do not enter into any commitments for material expenditures). The foregoing matters raise substantial doubt about our ability to continue as a going concern. See note 2 to the audited financial statements for the year ended December 31, 2004 and the explanatory notes included as part of this report, and *Liquidity And Capital Resources* below relating our plans to address our anticipated capital deficiency.

**Results of Operations**

We incurred a net loss before preferred dividends of $6,966,243 for fiscal 2004, as compared to $5,311,377 for fiscal 2003. The $1,654,866 or 31% increase in our net loss for fiscal 2004 before preferred dividends was attributable to a $1,165,731 increase in research and development expenditures, a $254,998 increase in net other expense, and a $234,137 increase in general and administrative expense.

Research and development expenditures for fiscal 2004 were $1,663,362, as compared to $497,631 for fiscal 2003. The $1,165,731 or 234% increase in research and development expenditures reflected the continued ramp-up in our research and development activities, including the addition of engineering personnel. The primary components of the increase for fiscal 2004 over 2003 were the expenditure of $688,286 for development costs to complete our Model 100 Module prototype; and an increase in $501,009 in compensation relating to research and development activities. These increases were partially offset by a net decrease in other expenditures.

General and administrative expenses for fiscal 2004 were $5,052,580, as compared to $4,818,443 for fiscal 2003. The primary components of general and administrative expenses during fiscal 2004 were legal fees, general consulting fees, settlement costs and investment banking fees. The $234,137 or 5% increase in general and administrative expenses was principally attributable to a $684,453 increase in consulting fees, a $576,585 increase in litigation settlement costs, and a $449,920 increase in legal fees for fiscal 2004 over 2003, partially offset by a $723,053 reduction in investment banking fees and a $722,352 decrease in employee and director stock and option compensation expense for fiscal 2004 over 2003. The principal component of the aforesaid litigation settlement costs was a non-cash expense of $757,202 reflecting the grant of a warrant to purchase 250,000 common shares at $7.90 per share, and does not take into consideration the value of 369,000 common shares surrendered as part of such settlement.

We incurred net other expense in the amount of $250,301 in fiscal 2004, as compared to $4,697 of income in fiscal 2003. Other net expense for fiscal 2004 was principally composed of interest and warrant repricing costs of $304,121, partially offset by interest income of $53,820.

We also incurred preferred dividend expense of $295,452 for fiscal 2004, as compared to $1,953,170 for fiscal 2003. The $1,657,718 or 85% decrease in preferred dividend expense was principally attributable to one-time charges of $896,474 and $949,121 in fiscal 2003 relating to the value of the beneficial conversion feature of preferred shares and the fair value of warrants issued with the preferred shares, respectively, issued during that year.

Our net loss attributable to common stockholders decreased from $7,264,547 for fiscal 2003 to $7,261,695 for fiscal 2004. The $2,852 decrease in net loss attributable to common stockholders was principally due to the $1,657,718 decrease in preferred dividend expense, partially offset by the aforesaid $1,654,866 increase to our net loss before preferred dividends.

**Plan of Operation**

Our plan of operation for the twelve month period following the date of this report is to (1) commence marketing our Model 100 Monitor System, (2) continue research and development activities relating to the development of our Model 200 Monitor System; (3) continue the evaluation process relating to establishment or acquisition of patient monitoring centers and, if the decision is made to proceed with these activities, to commence such activities; (4) to continue the investigation and potential development of our patient electrode vest and enhanced electrodes product ancillaries; and (5) complete initial studies relating to the applicability of our technology to the EEG market. We currently have budgeted $4,500,000 in costs for the twelve month period following the date of this report, including (1) $1,500,000 to cover our projected general and administrative expenses during this period; (2) $3,000,000 to cover our projected research and development, product testing and pre production engineering costs.

Described below are the company s various research and development, testing and pre production engineering projects and activities that are currently in progress or which we anticipate will commence during the twelve month period following the date of this report. As noted below, we anticipate that several of these projects or activities will not be completed until after the twelve month period cited. Since the anticipated overall cost of each of these later-completed projects or activities cited below necessarily include costs anticipated to be incurred after the end of the twelve month period cited, please note that the aggregate costs for all of the projects and activities cited below exceed the $3,000,000 budgeted as stated above. Our ability to perform the following activities will be based upon our available capital resources, and these activities will be reduced to the extent such resources are not available.

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We intend to finalize our selection of an ECG analysis software system that we will recommend for use with our Model 100 Module, as well as the necessary integration engineering to ensure that our Model 100 Module reliably and accurately produces signal data in a format compatible with that software. We anticipate we will spend approximately $50,000 to $250,000 to purchase the selected software packages, and an additional $20,000 to conduct the requisite integration engineering and testing activities. We anticipate we will identify and purchase the software and complete the integration engineering and testing activities by the third quarter of 2005. The foregoing does not include any additional expenditures or time required to modify the aforesaid standard software should that become necessary.

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We intend to conduct product performance studies comparing our Model 100 Monitor System against top-end ECG systems in order to identify and optimize the performance, usability and aesthetic aspects of our Model 100 Monitor System for marketing purposes. This testing will be conducted at our on-site laboratory facility. A minor expense of the testing plan will be the cost to acquire competitive devices. We have budgeted $28,000 for this phase, and have reached an oral agreement with Coast IRB, LLC to conduct our first user preference test at a date to be determined at a cost of $2,500.

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We intend to make arrangements with four or more hospitals, clinics or research institutions to evaluate our monitor system in a patient setting, in order to identify and optimize the performance, usability and aesthetic aspects of our Model 100 Monitor System for marketing purposes. Our anticipated budget for these activities is $400,000, including $92,000 to be paid to the Duke Clinical Research Institute with respect to the first pending evaluation of 50 to 90 patients. We anticipate that this study will be completed in August 2005, and the results published in November 2005. We are currently in the process of arranging a second patient study through the Cleveland Clinic, and anticipate developing a protocol for this study in the second quarter of 2005.

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In order to generate product awareness for our Model 100 Monitor System, we also intend to exhibit at trade shows and coordinate the writing of a number of technical papers relating to the effectiveness of our monitor system and to publish the results in peer review journals. The papers will also be presented at technical conferences and/or published in peer-reviewed scientific and medical journals. We have budgeted $100,000 for this phase.

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We must finalize third-party contract manufacturing arrangements to fabricate our Model 100 Module.

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We also intend to continue research and development activities with respect to our Model 200 Monitor System, patient monitoring centers and continuous preventative monitoring software project. With respect to the development of the Model 200 Module that will be the core feature of the Model 200 Monitor System, we have budgeted $2,815,000 to design, fabricate and test a pre-production model of this product under our research and development services agreement with Battelle Memorial Institute. The aforesaid estimate does not include the cost to establish or acquire patient monitoring centers.

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We also intend to continue investigation and development work on our patient vest. We project that we will spend approximately $230,000 to conduct these development activities, and expect to complete them by the last quarter of 2005.

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We will complete initial studies relating to the applicability of our technology to the EEG market. We project that we will spend approximately $84,000 to conduct these development activities, and expect to complete them by mid-2006.

Included in our anticipated general and administrative expenses for the twelve month period following the date of this report is $395,000 in marketing expenses. We intend during the twelve month period following the date of this report to expend a portion of our marketing budget on: (1) hiring three sales managers by the end of 2005 for the East Coast, Midwest, and South ($100,000); (2) exhibiting at various trade shows, including shows for the North American Society for Pacing and Electrophysiology, American College of Cardiology and American Heart Association to be held in 2005 ($30,000); (3) commencing an advertising program in cardiology journals in 2005 ($20,000); and (4) providing sample heart monitor systems to key cardiologists, hospitals and monitoring centers in early to mid-2005 ($15,000). The balance of the $395,000 will be spent on wages for current personnel ($160,000) and on miscellaneous marketing expense ($70,000).

We anticipate that we will add five additional employees to our staff during the twelve month period following the date of this report, comprised of the three regional sales managers noted above, a permanent chief financial officer who will replace our outside interim chief financial officer who we currently engage on a part-time contract basis, and a chief operating officer.

We can give you no assurance that we will be successful in developing our modules, patient vest or enhanced electrodes at all or within the timeframes or at the costs estimated, or in procuring FDA approval or clearance for these products when necessary, or in designing and engineering durable, reliable and competitively priced production versions of any of these products.

Our anticipated costs and project completion dates described above are estimates based upon our current business plan. Our actual costs or actual project completion dates could vary materially from those estimated. We may also decide at any time to terminate our ongoing development plans with respect to ancillary products such as our patient vests, enhanced electrodes and proprietary software should we deem them to be impracticable or not be commercially viable. Further, change to our current business plan could also result, such as the acquisition of new products or services or the decision to manufacture our own products, resulting in a change in our anticipated. See that section of this report captioned *Forward-Looking Statements* . At present, no changes to our business plan are being considered, nor is it our plan to change our business plan.

**Liquidity and Capital Resources**

As reported in our audited financial statements for the year ended December 31, 2004 included as part of this report, for the period January 1, 2003 through December 31, 2004, we principally financed our operations through a combination of (1) gross proceeds from contributed capital, the sale of our common shares, series A preferred shares and common share purchase warrants for cash, and the exercise of stock purchase warrants for cash ($6,301,645); (2) the issuance of common shares or common share purchase warrants in payment of the provision of services ($5,725,546); and (3) gross proceeds from the sale of a debenture and common share purchase warrants ($2,000,000). Included in the foregoing are the following significant transactions:

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From October through December 2003, we raised $5,378,650 in gross proceeds from a private placement to 100 investors effected through Maxim Group, LLC, a registered broker-dealer, as placement agent, pursuant to which we sold 1,792,976 series A convertible preferred shares, with each share convertible into one common share; and 896,488 Class C warrants, each warrant entitling the holder to purchase one common share for $3.75 (later voluntarily reduced by the company to $3).

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On December 29, 2004, we sold an 8% convertible debenture in the amount of $2,000,000 to DKR SoundShore Oasis Holding Fund Ltd. Subject to our right to convert the debenture into common shares as discussed below, we are obligated to pay $400,000 in principal on the debenture in cash on May 16, 2005, June 1, 2005, July 1, 2005, August 1, 2005 and August 31, 2005, respectively. We are also obligated to pay 8% in interest on the outstanding principal on the debenture in cash on May 10, 2005, June 1, 2005, July 1, 2005, August 1, 2005 and August 31, 2005, respectively. On January 26, 2005, we filed a registration statement to register common shares issuable upon the conversion of the debenture as discussed below, and it was declared effective by the SEC on February 14, 2005. Accordingly, under the terms of the debenture we are also entitled to pay the principal and interest on the debenture in common shares in lieu of cash so long as we are not otherwise in default under the debenture, and have satisfied certain other conditions including notice requirements.

For so long as the debenture is unpaid, the debenture holder is entitled to convert the debenture into a number of common shares equal to the outstanding principal on the debenture divided by $5.25, such amount representing 105% of the closing price for our common shares on the trading day prior to the sale of the debenture.

Should we elect to make payment in common shares as provided above, the principal and interest under the debenture subject to conversion would be convertible into those shares at the rate of 85% of the average of the three lowest closing prices for those shares during the ten day period prior to the repayment date. If we only elect to pay interest with common shares, the conversion rate shall be fixed at 90% of the closing price immediately prior to the payment or delivery date.

While we are not generally allowed to pre-pay the debenture before its August 31, 2005 due date without the consent of the debenture holder, we may do so in cash so long as we pay the entire outstanding balance due through maturity and also pays a 10% premium on the outstanding principal.

In the event of our default under the debenture, including both our failure to make principal and interest payments and our failure to comply with various covenants, the interest rate will increase to 15%, and we will be obligated to pay the greater of (1) the principal due under the debenture together with a 30% premium, plus interest accrued; or (2) the principal due under the debenture, plus interest accrued, divided by conversion price were the debenture holder to elect to convert the debentures into company common shares.

As additional consideration for the purchase of the debenture, we also granted to the debenture holder warrants entitling it to purchase 275,000 common shares at the price of $5.75 per share, or 115% of the closing price for those shares on the trading day prior to the sale of the debenture. These warrants lapse if unexercised by December 29, 2009. As the result of such grant, we have recorded a non-cash deferred financing charge in the amount of $447,570 reflecting the fair value attributable to these warrants. We have also recorded a non-cash beneficial conversion feature of $408,333, based upon the difference in the effective conversion price of the debenture and the closing price of our common stock on the date of issuance. As a result of these non-cash charges the effective annual rate of interest on the debenture is 89%.

Assuming we elect to convert the full $2,000,000 in outstanding principal on the debenture described above into common shares, we estimate that we will have sufficient cash on hand to fund our anticipated costs through August 2005 (assuming we reduce our expenditures to minimal levels and do not enter into any commitments for material expenditures). Should our costs and expenses prove to be greater than we currently anticipate, or should we change our current business plan in a manner that will increase or accelerate our anticipated costs and expenses, such as through an acquisition of new products, the depletion of our working capital would be accelerated. Once we commence marketing our patient modules as part of our monitor systems, we will nevertheless continue to be cash flow negative due to our costs exceeding our revenues for an indefinite period of time. We will need to raise additional cash and working capital to cover the shortfall in our cash and working capital anticipated to occur by August 2005 until such time, if at all, we become cash-flow positive. We will seek to raise this additional cash and working capital through the public or private sales of debt or equity securities, the procurement of advances on contracts or licenses, funding from joint-venture or strategic partners, debt financing or short-term loans, or a combination of the foregoing. We may also seek to satisfy indebtedness without any cash outlay through the private issuance of debt or equity securities. We currently do not have any binding commitments for, or readily available sources of, additional financing. We cannot give you any assurance that we will be able to secure the additional cash or working capital we may require to continue our operations.

**Critical Accounting Policies**

Our discussion and analysis of our financial condition and results of operations are based upon our financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States of America. The preparation of these consolidated financial statements requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosures of contingent assets and liabilities. For a description of those estimates, see note 2, *Significant Accounting Policies*, contained in the explanatory notes to our audited financial statements for the year ended December 31, 2004 included as part of this report. On an ongoing basis, we evaluate our estimates, including those related to reserves, deferred tax assets and valuation allowance, impairment of long-lived assets, fair value of equity instruments issued to consultants for services and estimates of costs to complete contracts. We base our estimates on historical experience and on various other assumptions that we believe to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying value of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions; however, we believe that our estimates, including those for the above-described items, are reasonable.

**Recent Accounting Pronouncements**

In November 2004, the FASB issued SFAS No. 151, *Inventory Costs, an amendment of ARB No. 43, Chapter 4*. The amendments made by Statement 151 clarify that abnormal amounts of idle facility expense, freight, handling costs, and wasted materials (spoilage) should be recognized as current period charges and require the allocation of fixed production overheads to inventory based on the normal capacity of the production facilities. The guidance is effective for inventory costs incurred during fiscal years beginning after June 15, 2005. Earlier application is permitted for inventory costs incurred during fiscal years beginning after November 23, 2004. Recom has evaluated the impact of the adoption of SFAS 151, and does not believe the impact will be significant to the company's overall results of operations or financial position since Recom currently does not have any manufacturing operations or inventory.

In December 2004, the FASB issued SFAS No.152, *Accounting for Real Estate Time-Sharing Transactions, an amendment of FASB Statements No. 66 and 67 (SFAS 152)* . The amendments made by Statement 152 amend FASB Statement No. 66, *Accounting for Sales of Real Estate* , to reference the financial accounting and reporting guidance for real estate time-sharing transactions that is provided in AICPA Statement of Position (SOP) 04-2, *Accounting for Real Estate Time-Sharing Transactions* . This Statement also amends FASB Statement No. 67, *Accounting for Costs and Initial Rental Operations of Real Estate Projects* , to state that the guidance for (1) incidental operations and (2) costs incurred to sell real estate projects does not apply to real estate time-sharing transactions. The accounting for those operations and costs is subject to the guidance in SOP 04-2. This statement is effective for financial statements for fiscal years beginning after June 15, 2005, with earlier application encouraged. Recom has evaluated the impact of the adoption of SFAS 152, and does not believe the impact will be significant to the company's overall results of operations or financial position since Recom does not enter into such transactions.

In December 2004, the FASB issued SFAS No.153, *Exchanges of Nonmonetary Assets, an amendment of APB Opinion No. 29, Accounting for Nonmonetary Transactions*. The amendments made by Statement 153 are based on the principle that exchanges of nonmonetary assets should be measured based on the fair value of the assets exchanged. Further, the amendments eliminate the narrow exception for nonmonetary exchanges of similar productive assets and replace it with a broader exception for exchanges of nonmonetary assets that do not have commercial substance. Previously, Opinion 29 required that the accounting for an exchange of a productive asset for a similar productive asset or an equivalent interest in the same or similar productive asset should be based on the recorded amount of the asset relinquished. Opinion 29 provided an exception to its basic measurement principle (fair value) for exchanges of similar productive assets. The FASB believes that exception required that some nonmonetary exchanges, although commercially substantive, be recorded on a carryover basis. By focusing the exception on exchanges that lack commercial substance, the FASB believes this statement produces financial reporting that more faithfully represents the economics of the transactions. SFAS 153 is effective for nonmonetary asset exchanges occurring in fiscal periods beginning after June 15, 2005. Earlier application is permitted for nonmonetary asset exchanges occurring in fiscal periods beginning after the date of issuance. The provisions of SFAS 153 shall be applied prospectively. Recom has evaluated the impact of the adoption of SFAS 153, and does not believe the impact will be significant to the company's overall results of operations or financial position.

In December 2004, the FASB issued SFAS No.123 (revised 2004), *Share-Based Payment* . SFAS 123(R) will provide investors and other users of financial statements with more complete and neutral financial information by requiring that the compensation cost relating to share-based payment transactions be recognized in financial statements. That cost will be measured based on the fair value of the equity or liability instruments issued. SFAS 123(R) covers a wide range of share-based compensation arrangements including share options, restricted share plans, performance-based awards, share appreciation rights, and employee share purchase plans. SFAS 123(R) replaces FASB Statement No. 123, *Accounting for Stock-Based Compensation* , and supersedes APB Opinion No. 25, *Accounting for Stock Issued to Employees* . SFAS 123, as originally issued in 1995, established as preferable a fair-value-based method of accounting for share-based payment transactions with employees. However, that statement permitted entities the option of continuing to apply the guidance in Opinion 25, as long as the footnotes to financial statements disclosed what net income would have been had the preferable fair-value-based method been used. Public entities (other than those filing as small business issuers) will be required to apply SFAS 123(R) as of the first interim or annual reporting period that begins after June 15, 2005. SFAS 123(R) is applicable for Recom effective the first interim period that starts after December 15, 2005. Recom has evaluated the impact of the adoption of SFAS 123(R), and believes that the impact will be significant to the company's overall results of operations and financial position (a pro forma effect, as estimated by management, is disclosed in note 2 of our financial statements).

In December 2004 the Financial Accounting Standards Board issued two FASB Staff Positions FSP FAS 109-1, *Application of FASB Statement 109 "Accounting for Income Taxes" to the Tax Deduction on Qualified Production Activities Provided by the American Jobs Creation Act of 2004,* and FSP FAS 109-2 *Accounting and Disclosure Guidance for the Foreign Earnings Repatriation Provision within the American Jobs Creation Act of 2004.* Neither of these affected the Company as it does not participate in the related activities

In January 2003, the FASB issued FASB Interpretation No. ("FIN") 46, "Consolidation of Variable Interest Entities" ("FIN 46"). In December 2003, FIN 46 was replaced by FASB interpretation No. 46(R) "Consolidation of Variable Interest Entities." FIN 46(R) clarifies the application of Accounting Research Bulletin No. 51, "Consolidated Financial Statements," to certain entities in which equity investors do not have the characteristics of a controlling financial interest or do not have sufficient equity at risk for the entity to finance its activities without additional subordinated financial support from other parties. FIN 46(R) requires an enterprise to consolidate a variable interest entity if that enterprise will absorb a majority of the entity's expected losses, is entitled to receive a majority of the entity's expected residual returns, or both. FIN 46(R) is effective for entities being evaluated under FIN 46(R) for consolidation no later than the end of the first reporting period that ends after March 15, 2004. The Company does not currently have any variable interest entities that will be impacted by adoption of FIN 46(R).

## MANAGEMENT

### Identity

The following table identifies our current executive officers and directors, their respective offices and positions, and their respective dates of election or appointment:

| Name And Municipality Of Residence | Age | Office | Initial Election Or Appointment Date |
| --- | --- | --- | --- |
| Lucy Duncan-Scheman<br>Washington, D.C. | 51 | Chairman of the Board and Director | March 22, 2005 |

Lowell T. Harmison, Ph.D.
Washington, D.C.

67

Chief Executive Officer and Director

June 6, 2003

Rodney Hildebrandt
Loveland, Ohio

56

Chief Operating Officer, Secretary and Director

March 22, 2005

Budimir S. Drakulic, Ph.D.
Los Angeles, California

54

Vice President and
Chief Technology Officer

October 15, 2002

Robert C. Scherne
Syosset, New York

48

Interim Chief Financial Officer

January 12, 2005

Ellsworth Roston
Los Angeles, California

81

Director

November 1, 2002

Jennifer Black
Lake Oswego, Oregon

48

Director

January 20, 2004

Pamela Bunes
Greenville, South Carolina

42

Assistant Secretary and Director

Messrs. Harmison, Hildebrandt and Drakulic provide their services as executive officers on a full-time permanent basis. Mr. Scherne provides his services on a part-time interim leased basis through Robert C. Scherne, CPA, PC, a company that specializes in providing financial management personnel to businesses on a temporary basis. On average, Mr. Scherne and the company anticipate that Mr. Scherne will devote between 5-25% of his time, or two to fifteen hours per week, to Recom depending upon the nature of the financial projects he is working on.

There are no family relationships between any two or more of our directors or executive officers. There is no arrangement or understanding between any of our directors or executive officers and any other person pursuant to which any director or officer was or is to be selected as a director or officer, and there is no arrangement, plan or understanding as to whether non-management shareholders will exercise their voting rights to continue to elect the current board of directors. There are also no arrangements, agreements or understandings to our knowledge between non-management shareholders that may directly or indirectly participate in or influence the management of our affairs.

**Business Experience**

***Lucy Duncan-Scheman*** has served as the Chairman of the Board and a director since March 22, 2005. Ms. Duncan-Scheman has served as President and Chief Executive Officer of Diplomatic Resolutions, Inc., an international business development consulting firm which she founded, since 1992. Ms. Duncan-Scheman has also served as President and Chief Executive Officer of Safe Ports, a subsidiary of Diplomatic Resolutions, since November 2003, and as President of Safe Ports Mexico since September 2004. Ms. Duncan-Scheman has served as President of the Board of Directors of the Washington Symphony Orchestra (1995 -2000), President, Museum of the Americas (2000-2003), Member Board of Directors of the National Chapter of Youth Service America (2000-2003), Council of World Regions (Brussels) 1994 - 1999, and The Pan American Development Foundation 2000-2001. Ms. Duncan-Scheme attended New York Institute of Technology.

***Dr. Lowell T. Harmison*** has served as Chief Executive Officer since March 26, 2005, and as a director since June 6, 2003. Dr. Harmison has also served as a Senior Advisor since February of 2003. Dr. Harmison has a very distinguished 35 year career in the field of biomedicine. Most recently, Dr. Harmison has served as a director and as chairman of the board of World Doc Foundation, a private foundation promoting health education and expanded knowledge of telemedicine, since June 2002. Dr. Harmison has also served as a director and chief executive officer of ProCell Corporation, a cancer research company, since June 2000, and as a director of pHA Bio Remediation, an environmental restoration company, since 1997. Dr. Harmison also served as chairman of Sequella Foundation, which promotes research into tuberculosis, from 1997 to 2001, and served as a director of Sequella Inc., a research and development company for tuberculosis products, from 1997 to 2000. Dr. Harmison is the holder of the first domestic and foreign patents on the fully implantable artificial heart; and served as Chief Executive Officer of USET, Inc. from 1987 to 1989. Dr. Harmison also served as the Director of the Robert Maxwell Foundation, a private foundation operating internationally and consisting of 21 operating companies, from 1987 to 1989. He also served as the Principal Deputy Assistant Secretary for Health of the U.S. Public Health Service, Department of Health and Human Services. Dr. Harmison has a Ph.D. from the University of Maryland and a B.S. and M.S. from West Virginia University. He was also given an honorary Doctor of Science degree from the West Virginia University.

***Rodney Hildebrandt*** has served as our Chief Operating Officer and as a director since March 22, 2005 and as Secretary since March 26, 2005. Prior to joining us, Mr. Hildebrandt held various positions with subsidiaries of Johnson & Johnson (NYSE:JNJ) for over 20 years, most recently as Director, Sales Planning and Operations and then Director, Corporate Communications, of Ethicon Endo-surgery, Inc. from October 1991 to February 2004, Strategic Project Management and then Sales Management of Johnson & Johnson Medical Inc. from 1985 to October 1991, and Operations Management for Johnson & Johnson Domestic Operating Co. Mr. Hildebrandt holds a Bachelors of Science degree in Business Management from the University of South Dakota.

***Dr. Budimir S. Drakulic*** has served as our Vice President and Chief Technology Officer since October 15, 2002. Dr. Drakulic has more than 25 years of experience in the design, development and integration of hardware and software modules for biomedical microelectronics circuits and systems. From 1997 through February of 2002, Dr. Drakulic was research and development principal for Advanced Heart Technologies, Inc., and its predecessor Advanced Heart Monitoring. From February of 2002 until October 15, 2002 Dr. Drakulic was involved in independent research. Dr. Drakulic was the Consultant and Chief Scientist, Medical Device Business Unit for Teledyne Electronic Technologies from 1992 through 1997. Before that, he held numerous positions affiliated with the University of California at Los Angeles, including Visiting Assistant Professor with the Electrical Engineering Department and Director of the Microelectronics Development Lab at the Crump Institute for Medical Engineering. He holds a Bachelor of Science degree in electrical engineering from the University of Belgrade, Yugoslavia. He also holds a Masters degree and a Ph.D. in Electronic and Biomedical Engineering from the same university. Dr. Drakulic was the recipient of the Ralph and Marjorie Crump Prize for Excellence in Medical Engineering from

UCLA in 1985, and was a Research Fellow with the Crump Institute for Medical Engineering at UCLA. Dr. Drakulic filed a petition for bankruptcy in November 2001.

***Mr. Robert C. Scherne*** has provided his services as our interim Chief Financial Officer since January 12, 2005 on a leased basis through Robert C. Scherne, CPA, PC, a company that specializes in providing financial management personnel to businesses on a temporary basis. We are planning to recruit a full-time Chief Financial Officer. Mr. Scherne has been the principal of Robert C. Scherne, CPA, PC, since March 2003. Prior to that, Mr. Scherne was employed as an accountant by Merdinger, Fruchter Rosen and Company from December 1993 to December 2002; by Louis Sturz & Co. and its successor firm Grossman, Russo & Shapiro from July 1986 until November 2002; and by L.H. Frishkoff &Co. and its successor firm A. Uzzo &Co. from July 1978 to June 1986. Mr. Scherne holds a Bachelors of Business Administration degree in Accounting from Pace University (New York City), and is an active member of the American Institute of Certified Public Accountants and the New York State Society of Certified Public Accountants

***Mr. Ellsworth Roston*** has served as a director since November 1, 2002. Mr. Roston has practiced patent law since 1943, and currently serves as Of Counsel to the patent firm of Fulwider Patton Lee & Utecht since 1997. Mr. Roston has a history of assisting technology companies during their development stages. Most recently, Mr. Roston has served as a director of Natgram, Inc., an internet software developer, since 1998, Amerlin Inc., a pet house/kennel manufacturer, since 1996, and American Legal Net, a provider of legal forms, since April 2004. Mr. Roston also served as a director of Rokenbok Corporation, a toy manufacturer, from 1996 through February 2004, and of Dome Industries, an electronic hardware manufacturer, from 1991 through 2002. Mr. Roston was one of three founders of Brooktree Corporation, and served on its board of directors for 15 years until it was purchased by Rockwell Corporation in 1998. Mr. Roston received his undergraduate degree and his law degree from Yale University.

***Ms. Jennifer Black*** has served as a director since January 20, 2004. Ms. Black has been President of her own business, Jennifer Black & Associates, since September 2003. Her firm provides independent research for institutional clients. Previously, since 1979, Ms. Black was with Black & Co., where she was responsible for research coverage on the apparel and specialty retail industries. Ms. Black was President of Black & Co. when it was acquired by First Security Van Kasper in April 2000. Subsequently, Wells Fargo Securities acquired First Security Van Kasper in September 2000. Ms. Black left Wells Fargo Securities in September 2003. Ms. Black serves on the Governors Council of Economic Advisors for the State of Oregon, where she has been re-appointed to a second three-year term. Ms. Black attended Washington State and Portland State Universities.

***Pamela Bunes*** has served as a director since March 22, 2005 and as Assistant Secretary since March 26, 2005. Ms. Bunes has been employed by Biosense Webster, Inc., since August 2004. Prior to that, Ms. Bunes was employed as Executive Account Manager with Ethicon Endo-Surgery, Inc., having started as Account Manager of that company in October 1990 until her transfer to Biosense Webster. Biosense Webster and Ethicon Endo-Surgery are each subsidiaries of Johnson & Johnson (NYSE:JNJ). Prior to that, Ms. Bunes was a Corporate Loan Officer and Vice President from 1986 to October 1990, and Analyst for the Specialized Industries Mergers and Acquisitions Group (Banking) from 1985 to 1986, of First Union National Bank. Ms. Bunes has a Bachelors of Arts degree with double majors in Economics and Business Administration (Finance) from Converse College in Spartanburg, South Carolina.

**Board Of Directors**

Our bylaws set the authorized number of directors on our board of directors at not less than three nor more than nine, with the actual number fixed by a resolution of our board. As noted above, there are currently six directors serving on our board, Messrs. Roston, Harmison and Hildebrandt and Ms. Duncan-Scheman, Black and Bunes. All of the directors will serve until the next annual meeting of shareholders and until their successors are elected and qualified by our shareholders, both common and preferred, voting on a cumulative basis as one class, or until their earlier death, retirement, resignation or removal. Each of the directors other than Messrs. Harmison and Hildebrandt are independent directors as that term is defined by the SEC.

**Board Committees**

Our board of directors has established two committees to date, an audit committee currently comprised of Mr. Roston and Ms. Black, and a compensation committee currently comprised of Ms. Duncan-Scheman and Black and Mr. Roston. Upon the completion of the filing of this annual report, Ms. Duncan-Scheman will replace Mr. Roston on the audit committee. None of our directors serving on the audit committee have the requisite public company accounting background or experience to be considered an audit committee financial expert as that term is defined by the SEC. Due to our development stage status, we believe that the current members of the audit committee have the requisite financial background and experience to carry out their duties.

**Board Compensation**

Our recent compensation policy for our directors for service on the full board has been to compensate them through stock grants under our 2002 Stock Plan pursuant to a director s compensation policy adopted on February 6, 2003. Upon joining our board of directors, each member is granted an option to purchase 50,000 (pre-split and post-split) common shares, exercisable at its then trading price. These options are fully vested upon grant, and lapse in five years if not exercised. Each director will thereafter be granted options on an annual basis entitling him to purchase an additional 28,000 (post-split) common shares, which options will vest quarterly based upon the continued provision of services as a director, and lapse in five years if not exercised. The exercise price for these options will be fixed at current market price as of the date of grant. Following our April 11, 2003 stock split, our board determined to maintain the grants at 50,000 common shares post-split for grants to new directors insofar as it believed such number was an appropriate number of option shares after taking into consideration factors it deemed relevant. Our compensation committee will be re-evaluating director compensation following recent changes to the composition of our board on March 22, 2005.

Our current compensation policy for our directors for serving on our various committees to the board has been to compensate them through the grant of common share purchase options. Prior to January 3, 2005, each committee member was granted an option to purchase 2,000 common shares, exercisable at its then trading price, upon his or her appointment to a committee. Commencing January 3, 2005, the amount of the grant was increased to 10,000 shares for serving on the audit committee, and 5,000 shares for serving on the compensation committee, with the first grants being made effective as of that date. All committee options vest in four quarterly installments subject to attendance at least 90% of the committee meetings during that quarter, and lapse in five years if not exercised. Our compensation committee will be re-evaluating director compensation following recent changes to the composition of our board on March 22, 2005.

The following table described the common share purchase options granted to our directors as of March 25, 2005 as compensation for serving on our board and, if applicable, committees of our board.

| **Name** | **Grant Date** | **Common Shares Purchasable** | **Exercise Price** | **Expiration Date** |
|---|---|---|---|---|
| Ellsworth Roston(1) | 2/6/2003 | 150,000(3) | $ 0.88 | 2/5/2008 |
| | 11/3/2003 | | | |

28,000

$ 4.40

11/2/2008

4/1/2004

2,000

$ 6.00

3/31/2009

7/8/2004

2,000

$ 3.95

7/7/2009

11/1/2004

28,000

$ 2.90

10/31/2009

1/3/2005

10,000

$ 5.05

1/2/2010

1/3/2005

5,000

$ 5.05

1/2/2010

Dr. Lowell T. Harmison(2)

6/5/2003

50,000

$ 4.20

6/5/2008

6/6/2004

28,000

$ 6.25

6/5/2009

Jennifer Black

1/20/2004

50,000

$ 3.50

1/19/2009

4/1/2004

500(4)

$ 6.00

3/31/2009

1/3/2005

10,000

$ 5.05

1/2/2010

(4)

Excludes 450,000 common share purchase warrants unrelated to the provision of services as a director which were granted to Mr. Roston as compensation for providing consulting services. See *Business-Employment And Consulting Agreements With Management*.

(2)

Excludes 216,000 common share purchase warrants unrelated to the provision of services as a director which were granted to Dr. Harmison as compensation for providing consulting services. See *Business-Employment And Consulting Agreements With Management*.

(3)

50,000 shares pre-split.

(4)

Ms. Black was originally granted 2,000 options, however, 1,500 options lapsed upon her resignation from the audit committee effective July 8, 2004. Ms. Black subsequently rejoined the audit committee on January 3, 2005.

We do not currently provide our directors with cash compensation, although we do reimburse their expenses.

**Medical Advisory Board**

Recom has composed a board of medical advisors comprised of Drs. Lowell T. Harmison, Michael M. Laks, Mitchell W. Krucoff and Andrea Natale to provide strategic assistance in the design, development and marketing of our medical devices.

***Dr. Lowell T. Harmison, Ph. D.,*** is a member of Recom s board of directors, and has served as a Senior Advisor since February of 2003. Dr. Harmison s background is provided earlier in this report in that section captioned *Business Experience* .

***Mitchell W. Krucoff, M.D., F.A.C.C., F.C.C.P.,*** who was appointed as a senior advisor in June 2004, is presently Associate Professor of Medicine/Cardiology at Duke University Medical Center, as well as the Director of eECG Core Laboratory and Interventional Device Trials at Duke Clinical Research Institute. Dr. Krucoff is a Fellow of the American College of Cardiology, on the Executive Committee of the International Society of Computerized Electrocardiology as well as a member of the Circulatory Devices Advisory Panel, U.S. FDA. Dr. Krucoff has published over 200 scientific and medical related papers. Dr. Krucoff received has bachelors degree from Yale University in 1976 and his medical degree from George Washington University in 1980.

***Andrea Natale, M.D.,*** who was appointed as a senior advisor in September 2004, is presently Professor of Medicine at the Ohio State University, and Program Director of the EP Fellowship Program at the Department of Cardiology of the Cleveland Clinic Foundation. Dr. Natale has been with the Ohio State University and the Cleveland Clinic

Foundation since 1999, having previously served as Director of Electrophysiology Laboratories of the Section of Electrophysiology and Pacing, then Co-Section Head of the Section of Electrophysiology and Pacing, and then as Medical Director, Center for Atrial Fibrillation. Previously, Dr. Natale was Associate Professor of Medicine at the University of Kentucky from 1997 to 1998, Assistant Professor of Medicine at the Duke University Medical Center and Director of the Electrophysiology Laboratory at the Durham Veterans Administration Medical Center from 1994 to 1997, and Head of the Cardiovascular Physiopathology Section of the Italian Air Force Aerospace Research Centre in Rome, Italy, from 1988 to 1989. Dr. Natale received his medical degree from the Medical School at the University of Florence, Italy.

**Senior Medical Advisors**

***Dr. Michael M Laks, M.D.,*** who has been a senior medical advisor to Recom since June 2003, is presently a Distinguished Professor of Medicine in the Division of Cardiology at the UCLA School of Medicine, Senior Physician at the Harbor-UCLA Medical Center, a reviewer for the New England Journal of Medicine, and Associate Editor of the Journal of Electrocardiology. Dr. Laks has published over 400 scientific and medical-related papers, and is a leading researcher in the field of computerized electrocardiography, with a research focus on microelectronics, cardiovascular system, bioengineering, electrophysiology, cardiovascular diseases, cardiology, automated clinical analysis, medical instrumentation, biotechnology and death and mortality, and having served as a consultant to Hewlett Packard on first computerized ECG program.

**Medical Advisor Compensation**

Each of the members of the medical advisory board and each senior medical advisor provide consulting services to Recom under consulting agreements and, as such, do not receive additional compensation for acting as a member of the medical advisory board.

Dr. Lowell T. Harmison is compensated for providing consulting services under an agreement dated February 14, 2003. For a description of the terms of that agreement see that section below captioned *Employment And Consulting Agreements With Management* .

Dr. Michael M. Laks is compensated for providing consulting services under an agreement dated June 2, 2003. Under that agreement, Dr. Laks received an initial grant of options entitling him to purchase 108,000 common shares at $2.40 per share, vesting over equally over four quarters, and cash compensation of $9,000 per quarter for the provision of up to 50 hours of consulting during that quarter. Any additional consulting services are compensated at the rate of $450 per hour.

Dr. Mitchell W. Krucoff is compensated for providing consulting services under an agreement dated May 26, 2004. Under that agreement Recom will pay Dr. Krucoff for his services the sum of $3,750 per quarter.

Dr. Natale is compensated for providing consulting services under a three-year agreement dated September 10, 2004. Under that agreement Recom will pay Dr. Natale for her services the sum of $4,500 per quarter.

**Other Significant Employees And Consultants**

***James J. Mazeika*** has served as our Director of Business Development since February 2004. Prior to joining Recom, Mr. Mazeika was Director of Strategic Marketing/Business Development for Bard Endoscopic Technologies from December 2002 to February 2004; President of his own consulting firm, Mazemac Group, from August 2001 to December 2002; Vice President/General Manager (Teledyne Medical) and then Vice President of Business Development (Medical Device Business Unit) of Teledyne Electronics Technologies, Inc., subsidiary of Teledyne Technologies, Inc. (NYSE:TDY); from December 1998 to August 2001; Product Manager (Catheters), Senior Market Manager (Devices) and ultimately Business Manager (Restenosis) of Mallinkrodt Medical from December 1991 to

December 1998; Research and Development Manager, Senior Project Engineer and ultimately Product Development Engineer with Bard Critical Care from November 1982 to December 1991, and Research Scientist for

The Kendall Company from July 1980 to November 1982. Mr. Mazeika holds a bachelors of science degree in biology from Loyola University (Chicago), a masters of science degree in biomedical engineering from the University of Illinois, and a masters of business administration degree from River College (Nashua, Hew Hampshire).

***William R. Matthews*** has served as our Director of Regulatory Affairs since July 2004. Prior to joining Recom, Mr. Matthews provided consulting services to Recom from December 2003 to July 2004, was Vice President, Government Affairs and Product Assurance for Viasys Healthcare (NYSE:VAS) from February 1999 to December 2003, was Executive Vice President, Operations, of Xylum Corporation from 1993 to 1998; was Corporate Director Engineering and Manufacturing, and ultimately Corporate Director, Product Assurance and Regulatory Affairs for W.R. Grace Company (NYSE:GRA) from 1987 to 1993; was Plant Manager for Beiersdorf, Inc. from 1981 to 1987; and Production Supervisor, R&D Supervisor and ultimately Production Superintendent for Best Foods Inc. from 1976 to 1981. Mr. Matthews holds a Bachelors of Science degree chemistry awarded by St. Peters University (New Jersey).

**Employment And Consulting Agreements With Management**

***Lowell T. Harmison, Chief Executive Officer and Director***

Dr. Lowell T. Harmison is currently employed as our Chief Executive Officer on an at-will basis. Dr. Harmison and our compensation committee are presently under discussion relating to the terms of an employment agreement with respect to the provision of these services, as well as addressing matters concerning the interplay with Dr. Harmison s consulting agreement as discussed below.

Dr. Harmison has previously provided consulting services to Recom under a three-year agreement dated February 14, 2003. Under this agreement, Dr. Harmison provides advice to us in the areas of technological support and strategy, product development, medical and scientific advisory board development, and FDA regulation. The compensatory terms of the agreement are as follows:

.

Recom is obligated to pay Dr. Harmison $36,000 per year over the term of the agreement, payable quarterly.

.

Dr. Harmison was entitled to receive upon execution of the agreement an initial grant of options entitling him to purchase 108,000 common shares (36,000 shares pre-split) at $0.97 per share, exercisable over five years.

.

Dr. Harmison was further entitled to receive upon execution of the agreement an additional grant of options entitling him to purchase 108,000 common shares (36,000 shares pre-split) at $0.97 per share, vesting in increments of 9,000 common shares each upon the first through twelfth quarterly anniversary dates of the agreement based upon his provision of services. These options are exercisable for a period of five years following vesting.

.

Dr. Harmison is entitled to receive grants of common share purchase options in tranches of 20,000 shares per milestone for assisting Recom in attaining various milestones determined by our board of directors, including the preparation and filing with the FDA of a 510(k) application for our product as it relates to its incorporation into a vest, approval of that application by the FDA, and market launch of that product.

.

Dr. Harmison is entitled to receive a grant of 20,000 common shares in the event of a change in control as that term is defined in the agreement.

On January 21, 2005, we entered into a second consulting agreement with Dr. Harmison in connection with the provision of his services in evaluating the applicability of our technology to the EEG market. Under this agreement, we acknowledged that Dr. Harmison had previously provided services for this project for which we compensated him with the sum of $70,000 in registered common shares, and that Dr. Harmison would provide an additional $84,000 in services, payable at the rate of $16,000 per month, to complete the project over a six month term.

***Rodney Hildebrandt, Chief Operating Officer and Secretary***

Mr. Hildebrandt is currently employed on an at-will basis. Mr. Hildebrandt and our compensation committee are presently under discussion relating to the terms of an employment agreement with respect to the provision of these services.

***Budimir Drakulic, Vice President and Chief Technology Officer***

On October 11, 2002, Recom reached an agreement-in-principle with Dr. Budimir Drakulic to become our Vice President and Chief Technology Officer on a consulting basis through his consulting companies. Pursuant to that understanding, on October 15, 2002, we entered into a loan-out agreement with B World Technologies, Inc. and B Technologies, Inc. relative to the provision of Dr. Drakulic s services, which formally commenced as of that date. Dr. Drakulic is the president and owner of these companies. The essential terms of the loan-out agreement are as follows:

.

The agreement provides for a ten-year initial term. After the initial term, the agreement renews automatically for successive one year terms, unless either party delivers 90-days written notice to the other of their intent not to renew.

.

Dr. Drakulic s services are provided on a mutually-acceptable part-time basis.

.

Recom is obligated to pay B Technologies a $10,000 bonus upon execution, and a monthly service fee of $15,000 thereafter.

.

B World Technologies was granted 600,000 restricted common shares (200,000 shares pre-split), to be earned over five years of continuous provision of services by Dr. Drakulic. These shares, which will be held in escrow with the company pursuant to the terms of a restricted stock agreement until they are earned, vest at the rate of 30,000 shares per quarter with the first 30,000 shares vesting on January 15, 2003. B World Technologies is entitled to all dividends which may be declared with respect to these shares, even if not vested.

The loan-out agreement provides for early termination should B World and B Technologies fail, neglect or refuse to provide Dr. Drakulic s services. In such an event, all compensation under the agreement will terminate and the unvested portion of the 600,000 restricted common share grant shall be deemed forfeit as of the effective termination date.

Since March 1, 2003, Dr. Drakulic has worked for us on a full-time basis even though the loan-out agreement only provides for the provision of part-time services. We have agreed to characterize these additional services as being provided by Dr. Drakulic as an employee, and to pay him $7,500 annually as compensation for their provision. Since January 1, 2004, this annual compensation was increased to $37,000.

On March 10, 2003, as additional incentive for the performance of Dr. Drakulic, we granted to B World Technologies options entitling it to purchase 750,000 common shares at $0.95 per share. These options vest quarterly over a four year term, and lapse, if not exercised, on March 9, 2008.

Concurrent with entering into the loan-out agreement, B World Technologies, B Technologies and Dr. Drakulic signed an employment, confidential information, invention assignment and arbitration agreement under which they agreed, among other things, to assign to us all of Dr. Drakulic s right, title and interest in and to any and all inventions, discoveries, etc. which he conceives or develops while engaged by Recom.

***Robert C. Scherne, Interim Chief Financial Officer***

Mr. Robert C. Scherne provides his services as Interim Chief Financial Officer on a leased basis through Robert C. Scherne, CPA, PC, a company that specializes in providing financial management personnel to businesses on a temporary basis. Under our engagement agreement with Robert C. Scherne, CPA, PC, we pay the company the sum of $150 per hour, subject to a cap of $15,000 with respect to the preparation of financial statements for each annual report on form 10-KSB or quarterly report on form 10-QSB.

***Ellsworth Roston, Director and Consultant***

On October 11, 2003, Recom reached an agreement-in-principle with Mr. Ellsworth Roston to provide consulting advice to us relating to engineering, developing and refining our products and technologies; to become a director of the company, and to make an investment into the company. Pursuant to that understanding, on October 30, 2002 we sold Mr. Roston 71,250 common shares (23,750 shares pre-split) for $190,000 in cash, and on November 1, 2002 we entered into a two year consulting agreement with Mr. Mr. Roston documenting the provision of his consulting services and his appointment to our board of directors. The agreement provides for us to grant to Mr. Roston 225,000 common shares (75,000 shares pre-split) and five-year warrants to purchase an additional 450,000 common shares (150,000 shares pre-split) at $1.67 per share. We consider the grant of common shares to Mr. Roston to be compensation for the provision of his consulting services, and the grant of the common share purchase warrants to be additional consideration for his cash investment pursuant to our original understanding.

Mr. Roston is a patent attorney whose law firm also handles our patent work. The agreement specifically provides that the consulting services provided by Mr. Roston will not include any legal work, for which we will compensate his law firm separately.

***Pamela Bunes, Assistant Secretary, Director and Consultant***

Ms. Bunes has agreed to provide consulting services to Recom. Ms. Bunes and our compensation committee are presently under discussion relating to the terms of a consulting agreement with respect to the provision of these services:

**Summary Compensation Table**

The following table shows the compensation paid over the past three fiscal years with respect to Recom s named executive officers as that term is defined by the SEC.

**Long Term Compensation**

**Annual Compensation (1)**

**Awards**

**Payouts**

**Named Executive Officer and Principal Position**

**Year**

**Salary**

**Bonus**

**Other**

**Restricted Stock**

**Securities Underlying Options & SARs**

**Long Term Incentive Plan**

**All Other Comp- ensation**

Marvin H. Fink (2)
*Chief Executive Officer*

2004
2003
2002

$ 1(5)
1(5)
1

$

$21,576(9)
19,598(10)

$

14,284(11)

178,000

$

$

Dr. Budimir Drakulic (3)
*Vice President and Chief Technology Officer*

2004
2003
2002

$ 207,105(6)
180,000(6)
45,000(6)

$

$

$

3,987(12)

750,000

$

$

Charles Dargan (4)
*Former Interim Chief Financial Officer*

2004
2003
2002

$ 75,000(8)
7,500(8)

$

$

$

$

$

(1)

Includes, among other things, perquisites and other personal benefits, securities or property which exceed in the aggregate the lesser of either $50,000 or 10% of the total annual salary and bonus reported for that fiscal year.

(2)

Mr. Fink served as our Chief Executive Officer from October 12, 2002 to March 22, 2005, and as our President from October 12, 2002 to March 28, 2005.

(3)

Dr. Drakulic has served as our Vice President and Chief Technology Officer since October 15, 2002.

(4)

Mr. Dargan served as our interim Chief Financial Officer from December 18, 2003 through January 12, 2005 on a leased basis through CFO 911, an agency that specializes in providing financial management personnel to businesses on a temporary basis.

(5)

Recom has recorded a non-cash accounting expense in the amount of $80,000 to reflect the value of Mr. Fink s services.

(6)

These amounts were paid in consulting payments to B Technologies in connection with its provision of Dr. Drakulic s services. Payment of a portion of these services in fiscal 2003 and 2004 were satisfied with common shares issued directly to Dr. Drakulic at the direction of B Technologies pursuant to the requirements of a registration statement on form S-8.

(7)

Includes the grant of 39,087 registered common shares with a value of $164,389.

(8)

Amounts paid to CFO 911.

(9)

Includes $14,400 in automobile allowance payments and $7,176 in premiums payable on health insurance.

(10)

Includes $14,400 in automobile allowance payments and $5,598 in premiums payable on health insurance.

(11)

Reflects the value of an award to Mr. Fink of 2,100,000 restricted common shares (700,000 shares pre-split) in conjunction with the execution of his employment agreement dated October 12, 2002. The value cited is based upon the closing price for on common shares as of the date of the employment agreement. As of December 31, 2004, all 2,100,000 restricted common shares remained outstanding. The value of those shares as of that date was $10,605,000 based upon the $5.05 closing price for our common shares as quoted on the OTCBB for December 31, 2004.

(12)

Reflects the value of an award to B. World Technologies of 600,000 restricted common shares (200,000 shares pre-split) in conjunction with the execution of a loan-out agreement dated October 12, 2002 by which it provided the services of Dr. Drakulic to Recom. The value cited is based upon the closing price for on common shares as of the date of the loan-out agreement. As of December 31, 2004, all 600,000 restricted common shares remained outstanding. The value of those shares as of that date was $3,030,000 based upon the $5.05 closing price for our common shares as quoted on the OTCBB for December 31, 2004.

**Stock Options And Stock Appreciation Rights Grant Table**

The following table provides certain information with respect to individual grants during the 2004 fiscal year to each of our named executive officers of common share purchase options or stock appreciation rights relating to our common shares:



---

| Name | Common Shares Underlying Grant Of Options Or SARs | As Percentage Of Grants To All Employees(1) | Exercise Or Base Price | FMV At Grant Date | Expiration Date |
|---|---|---|---|---|---|
| Marvin H. Fink | 2,000 | 1.8% | $6.00 | $6.00 | March 31, 2009 |
| Marvin H. Fink | 28,000 | 25.5% | $02.29 | $02.29 | October 11, 2009 |
| Dr. Budimir S. Drakulic | | | | | |

Charles Dargan

(1)

The numerator in calculating this percentage includes common share purchase options granted to each named executive officer in fiscal 2004 in his capacity as an officer or employee and, if applicable, as a director. The denominator in calculating this percentage is 110,000, which represents options granted to all Recom employees during fiscal 2004, including those to the named executive officers.

**Stock Options And Stock Appreciation Rights Exercise And Valuation Table**

The following table provides certain information with respect to each of our named executive officers concerning any common share purchase options or stock appreciation rights they may have exercised in fiscal 2004, and the number and value of any unexercised common share purchase options or stock appreciation rights they may hold as of December 31, 2004:

| | | | Unexercised In-The-Money Options and SARs at December 31, 2004 |
|---|---|---|---|
| **Named Executive Officer** | **Shares Acquired On Exercise** | **Value Realized (1)** | |

| | Number (Exercisable/ Unexercisable) | Value (2) (Exercisable/ Unexercisable) |
|---|---|---|
| Marvin H. Fink | 178,000 / 28,000 | $742,260 / $116,760 |
| Dr. Budimir S. Drakulic | 328,125 / 421,875 | $1,355,156 / $1,742,344 |
| Charles Dargan | / | / |

(2)

The dollar amount shown represents the difference between the fair market value of our common stock underlying the options as of the date of exercise and the option exercise price.

(2)

The dollar value provided represents the cumulative difference in the fair market value of our common stock underlying all in-the-money options as of December 31, 2004 and the exercise prices for those options. Options are considered in-the-money if the fair market value of the underlying common shares as of the last trading day in fiscal 2004 exceeds the exercise price of those options. The fair market value of Recom common shares for purposes of this calculation is $5.05, based upon the closing price for our common shares as quoted on the OTCBB on December 31, 2004.

**Compliance With Section 16**

None of our securities have been registered on a national securities exchange within the meaning of Section 12(b) of the Exchange Act, nor are they required to be registered under Section 12(g) of the Exchange Act. Accordingly, our executive officers, directors and affiliates are not presently subject to compliance with Section 16 of the Exchange Act.

**Code of Ethics**

Our Board of Directors adopted a code of ethics on January 20, 2004, which applies to all of our officers, directors and employees. This code may be found in pdf format on our corporate website at www.recom-systems.com.



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**PRINCIPAL SHAREHOLDERS**

The following table sets forth selected information, calculated as of March 25, 2005, about the amount and nature of our securities beneficially owned by each of (1) our *executive officers*, defined as our President, Secretary, Chief Financial Officer or Treasurer, any vice-president in charge of a principal business function, such as sales, administration or finance, or any other person who performs similar policy making functions for our company; (2) each of our directors; (3) each person known to us to own beneficially more than 5% of any class of our securities; and (4) the group comprised of our current directors and executive officers.

The number and percentage of shares beneficially owned is determined in accordance with Rule 13d-3 and 13d-5 of the Securities Exchange Act of 1934, as amended (the *Exchange Act*), and the information is not necessarily indicative of beneficial ownership for any other purpose. See footnote (1) to this table. We believe that each individual or entity named has sole investment and voting power with respect to the securities indicated as beneficially owned by them, subject to community property laws, where applicable, except where otherwise noted. Unless otherwise stated, the address of each person is 4705 Laurel Canyon Boulevard, Suite 203, Studio City, California 91607.

| | **Class Of Stock(1)** | | | |
|---|---|---|---|---|
| | **Common (Voting)** | | **Series A Preferred (2) (Voting)** | |
| **Name** | **Amount** | **%** | **Amount** | **%** |
| Dr. Lowell T. Harmison (3)(4) | 311,293(8) | * | 0 | — |
| Rodney Hildebrandt (3)(4) | 0 | — | 0 | |

| | | | | |
|---|---|---|---|---|
| | | | | — |
| Robert C. Scherne (4) | 0 | — | 0 | — |
| Dr. Budimir S. Drakulic (4) | 975,000(9) | 2.8% | 0 | — |
| Lucy Duncan-Scheman (3) | 1,230 | * | 0 | — |
| Ellsworth Roston (3) | 945,500(10) | 2.7% | 0 | — |
| Jennifer Black (3) | | | | |

| | | |
|---|---|---|
| | 53,000(11) | * |
| | 0 | — |
| Pamela Bunes (3) | 0 | — |
| | 0 | — |
| Tracey Hampton / ARC Finance Group, LLC (5)(6) | 22,950,000(12) | 65.4% |
| | 0 | — |
| Marvin H. Fink (5) | 2,295,250(13) | 6.5% |
| | 0 | — |
| Otape Investments LLC | 0 | — |

| | | |
|---|---|---|
| | 83,335 | 43.1% |
| Charles Hadad | 0 | — |
| | 18,328 | 9.5% |
| Roy G. Shaw Jr. | 0 | — |
| | 18,313 | 9.5% |
| Directors and executive officers, as a group | 4,634,273(14) | 12.6% |
| | 0 | — |

*

Less than one percent.

(1)

Pursuant to Rules 13d-3 and 13d-5 of the Exchange Act, beneficial ownership includes any shares as to which a shareholder has sole or shared voting power or investment power, and also any shares which the shareholder has the right to acquire within 60 days, including upon exercise of common shares purchase options or warrant or conversion of series A preferred shares. The number of outstanding shares of our common and series A preferred shares as of March 25, 2005 are 35,077,947 and 275,323 shares, respectively.

(2)

Each series A preferred share is convertible into one common share.

(3)

Director.

(4)

Executive officer.

(5)

5% shareholder.

(6)

The address of Ms. Hampton and ARC Finance Group LLC is 23679 Calabasas Road, Suite 754, Calabasas, CA 91302.

(7)

The address of Mr. Fink is 11500 West Olympic Boulevard,, Los Angeles, CA 90064.

(8)

Includes 216,000 common shares issuable upon exercise of warrants granted to Dr. Harmison in his capacity as a consultant, and 71,000 common shares issuable upon exercise of options granted to Dr. Harmison in his capacity as a director.

(9)

Includes 600,000 common shares held by B World Technologies, Inc., and 375,000 common shares issuable upon exercise of options granted to B World Technologies in connection with services performed by Dr. Drakulic. B World Technologies is owned and controlled by Dr. Drakulic.

(10)

Includes 296,250 common shares held by Roston Enterprises, 450,000 common shares issuable upon exercise of warrants granted to Mr. Roston in his capacity as a consultant, and 199,250 common shares issuable upon exercise of options granted to Mr. Roston in his capacity as a director.

(11)

Includes 53,000 common shares issuable upon exercise of options granted to Ms. Black in her capacity as a director.

(12)

Includes 22,950,000 common shares held by ARC Finance Group, Inc.  ARC Finance Group is owned and controlled by Ms. Hampton.

(13)

Includes 2,100,000 common shares held by the Fink Family Trust, and 195,250 common shares issuable upon exercise of options granted to Mr. Fink in his capacity as a director.

(14)

Includes 1,740,000 common shares issuable upon exercise of common share purchase options and warrants.

**TRANSACTIONS AND BUSINESS RELATIONSHIPS WITH MANAGEMENT AND PRINCIPAL SHAREHOLDERS**

**Transactions With Executive Officers, Directors And Shareholders**

Summarized below are certain transactions and business relationships between Recom and persons who are or were an executive officer, director or holder of more than five percent of any class of our securities since January 1, 2003:

.

On February 14, 2003, we entered into a three-year consulting agreement with Dr. Lowell T. Harmison, who later became one of our directors. Under the terms of that agreement, we granted to Dr. Harmison, among other things, (1) fully vested options entitling him to purchase 108,000 common shares (36,000 shares pre-split) at $0.97 per share, and (2) options entitling him to purchase an additional 108,000 common shares (36,000 shares pre-split) at $0.97 per share subject to vesting over twelve quarters. All of the aforesaid options are exercisable over five years after vesting. For a description of the full terms of that agreement see that section of this report captioned *Management Employment And Consulting Agreements With Management* .

.

On April 8, 2003, we sold to Mr. Mitchell Stein 112,812 common shares (37,604 shares pre-split) for $100,000 in cash and $150,000 in expenses and equipment. Mr. Stein is the spouse of Ms. Tracey Hampton, who owns and controls ARC Finance Group, LLC, which owns 65.4% of our outstanding common shares.

.

On May 15, 2003, we sold to Mr. Mitchell Stein 16,000 units at $3 per unit for cash amounting to $48,000. Each unit consisted of one common share and one warrant. Each warrant is exercisable at $3 until May 14, 2004. Upon exercise of the warrants, Mr. Stein will receive one common share and an additional warrant to purchase one common share $6 per share until November 15, 2004. The sale of units to Mr. Stein was part of a larger private placement on the same terms and conditions with two other investors. These warrants have since lapsed unexercised.

.

On July 24, 2003, we sold to Mr. Mitchell Stein 30,030 units at $3.33 per unit for cash amounting to $100,000. Each unit consisted of one common share and one warrant. Each warrant is exercisable at $3.33 until July 14, 2004. Upon exercise of the warrants, Mr. Stein will receive one common share and an additional warrant to purchase one common share at $6.66 per share until November 15, 2004. The sale of units to Mr. Stein was part of a larger private placement on the same terms and conditions with three other investors. These warrants have since lapsed unexercised.

**Parent Corporation**

ARC Finance Group, LLC, owns 65.4% of our outstanding common shares. ARC Finance Group is principally owned and controlled by Ms. Tracey Hampton. As a consequence, Ms. Hampton has the ability, through ARC Finance Group, to elect a majority of our board of directors, and thereby control our management. Ms. Hampton also has the ability to control the outcome of corporate actions requiring shareholder approval, including mergers and other changes of corporate control, going private transactions, and other extraordinary transactions.

## EQUITY COMPENSATION PLANS

**Summary Equity Compensation Plan Data**

The following table sets forth information compiled on an aggregate basis, with respect to equity compensation plans, including individual compensation arrangements as of December 31, 2004 under which we are granted or are authorized to issue equity securities to employees or non-employees in exchange for consideration in the form of goods or services:

| Plan Category | Number Of Securities To Be Issued Upon Exercise Of Outstanding Options, Warrants Or Rights | Weighted-Average Exercise Price Of Outstanding Options, Warrants And Rights | Number Of Securities Remaining Available For Future Issuance Under Equity Compensation Plans (Excluding Securities To Be Issued Upon Exercise Of Outstanding Options, Warrants And Rights) |
|---|---|---|---|
| Equity compensation plans approved by shareholders: | | | |
| Recom Managed Systems, Inc. 2002 Stock Plan | 2,100,000 | | |

$ 1.56

3,894,000

Equity compensation plans not approved by shareholders:

Recom Managed Systems, Inc. 2003 Nonqualified Stock Option And Stock Plan

Stand-alone grants

437,000

$

$ 2.50

707,843

Total

2,537,000

$ 1.72

4,601,843

**Description of Equity Compensation Plans Approved By Shareholders**

Recom has one equity compensation plan or arrangement that has been approved by our shareholders, the Recom Managed Systems, Inc. 2002 Stock Plan (the *2002 Stock Plan* ). Recom adopted the 2002 Stock Plan, pursuant to which 6,000,000 common shares (2,000,000 shares pre-split) were originally reserved for issuance, on November 1, 2002. Shareholder approval was received on June 5, 2003.

The 2002 Stock Plan was adopted by our board of directors as a vehicle to encourage and provide for the acquisition of an equity interest in Recom by our employees, officers, directors and consultants. Our board believes the plan will enable us to attract and retain the services of key employees, officers, directors and consultants upon whose judgment, interest and special effort the successful conduct of its operations is largely dependent, and to motivate those individuals by providing additional incentives and motivation toward superior performance.

The 2002 Stock Plan allows our board of directors, or a committee established by our board, to award restricted stock and stock options from time to time to our employees, officers, directors and consultants. The board has the power to determine at the time an option is granted whether the option will be an incentive stock option, which is an option which qualifies under Section 422 of the Internal Revenue Code of 1986, or an option which is not an incentive stock option. Incentive stock options may only be granted to persons who are our employees. Vesting provisions are determined by our board at the time options are granted. Options may be exercisable by the payment of cash or by other means as authorized by the committee or our board of directors.

The 2003 Stock Plan also provides that our board of directors, or a committee established by our board, may issue restricted stock pursuant to restricted stock right agreements which will contain such terms and conditions as our board or committee determines.

As of March 25, 2005, there were 2,094,000 common shares issued or reserved for issuance under the 2002 Stock Plan, and 3,906,000 common shares available for issuance.

**Description of Equity Compensation Plans Not Approved By Shareholders**

***2003 Stock Plan***

Recom has one formal stock plan considered to be an equity compensation plan or arrangement that has not been approved to date by our shareholders, the Recom Managed Systems, Inc. 2003 Nonqualified Stock Option And Stock Plan (the *2003 Stock Plan* ). Recom adopted the 2003 Stock Plan, pursuant to which 1,500,000 common shares (500,000 shares pre-split) were originally reserved for issuance, on March 31, 2003. The 2003 Stock Plan was adopted by our board of directors as a vehicle to encourage and provide for the acquisition of an equity interest in Recom by our employees, officers, directors and consultants. Our board believes the plan will enable us to attract and retain the services of key employees, officers, directors and consultants upon whose judgment, interest and special effort the successful conduct of its operations is largely dependent, and to motivate those individuals by providing additional incentives and motivation toward superior performance.

The 2003 Stock Plan allows our board of directors to grant stock options or issue stock from time to time to our employees, officers, directors and consultants. Options granted under the 2003 Plan do not qualify under Section 422 of the Internal Revenue Code as incentive stock options.

The 2003 Plan also provides that our board of directors, or a committee, may issue free-trading or restricted stock pursuant to stock right agreements containing such terms and conditions as our board of directors deems appropriate.

As of March 25, 2005, there were 857,593 common shares issued or reserved for issuance under the 2003 Stock Plan, and 642,407 common shares available for issuance.

On March 26, 2003, we filed with the SEC a registration statement on form S-8 for the purpose of registering the common shares issuable under our 2003 Stock Plan under the Securities Act. We have, to date, principally used the 2003 Stock Plan to grant registered common shares to selected consultants as compensation for services, while utilizing the 2002 Stock Plan for unregistered grants of stock and options to directors, officers, employees and other consultants.

***Stand-Alone Grants***

The stand-alone grant to Mr. Marvin Fink of 2,100,000 restricted shares under his employment agreement pursuant to which he agreed to become our Chief Executive Officer, President and Chairman of the Board; the stand-alone grant to B Technologies of 600,000 restricted common shares under the terms of the loan-out agreement by which we procured the services of Mr. Budimir S. Drakulic as our Vice President and Chief Technology Officer, and the stand-alone grant to Mr. Ellsworth Roston of 225,000 restricted common shares and warrants entitling him to purchase an additional 450,000 common shares under the terms of his consulting agreement with our company, each constitute an equity compensation plan or arrangement that has not been approved to date by our shareholders. For further information relating to these transactions, see that section of this report captioned *Management Employment And Consulting Agreements With Management* .

From time to time our board of directors grants common share purchase options or warrants to selected directors, officers, employees, consultants, advisors or vendors in payment of goods or services provided by such persons on a stand-alone basis outside of any of our formal stock plans. The terms of these grants are individually negotiated.

## UNCERTAINTIES AND RISK FACTORS THAT MAY AFFECT OUR FUTURE RESULTS AND FINANCIAL CONDITION

We have described below a number of uncertainties and risks which, in addition to uncertainties and risks presented elsewhere in this annual report, may adversely affect our business, operating results and financial condition. The

uncertainties and risks enumerated below as well as those presented elsewhere in this annual report should be considered carefully in evaluating our company and our business and the value of our securities.

**Risks Relating To Our Business**

***Our limited operating history will make it difficult for you to predict our future operating results and to otherwise assess or predict the likelihood of our business success.***

To date, we are a development stage company principally engaged in research and development, organizational and startup activities which has not yet introduced our heart monitoring products to market. Our limited operating history will make it difficult, if not impossible, to predict future operating results and to assess the likelihood of our business success in considering an investment in our company. Risks and issues inherent in the establishment and expansion of a new business enterprise which we face include, among others, problems of entering new markets, marketing new technologies, hiring and training personnel, acquiring reliable facilities and equipment, and implementing operational controls. As a development stage company, we are also subject to risks and or levels of risk that are often greater than those encountered by companies with established operations and relationships. Development stage companies often require significant capital from sources other than operations. Since we are a start-up business, our management and employees will shoulder the burdens of the business operations and a workload associated with company growth and capitalization that is disproportionately greater than that for an established business. We cannot give you any assurance that we will successfully address these risks. Our prospects must be considered speculative, which may limit our ability to encourage further investment in our company.

***We have no revenues to date and have accumulated losses since our inception. Our continued inability to generate revenues and profits could cause us to go out of business.***

We have incurred cumulative net losses after preferred dividends available to common shareholders in the amount of $14,421,842from our inception through December 31, 2004 and have debt of $2,000,000 maturing in increments by August 31, 2005. We have no commercial product sales or revenues to date, and do not anticipate that we will commence commercial sales of our heart monitoring products until early 2006. Once we commence marketing our heart monitoring products, we project that we will not be cash flow positive based solely on projected sales and service revenues less manufacturing, general and administrative, marketing expenses and other operating costs for an indefinite period of time. We anticipate that we will continue to incur substantial operating losses for the foreseeable future, notwithstanding any anticipated revenues we may receive when our products are initially introduced to markets, due to the significant costs associated with the development and marketing of our products and services.

***If we are unable to raise additional working capital, we will be unable to fully fund our operations and to otherwise execute our business plan, leading to the reduction or suspension of our operations and ultimately our going out of business.***

As of the date of this report and assuming the full conversion of an outstanding debenture in the amount of $2,000,000 into common shares, we will have sufficient cash on hand to our anticipated costs through August 2005 (assuming we reduce our expenditures to minimal levels and do not enter into any commitments for material expenditures), although this coverage could be less than that period as the result of changes in our anticipated level of operations, higher than expected costs such as through an acquisition of new products, or changes in our business plans. As noted in the prior risk factor, we do not anticipate that we will commence commercial sales of our heart monitoring products until early 2006, and further anticipate that after such introduction we will continue to be cash flow negative due to our costs exceeding our revenues for an indefinite period of time. Based upon the foregoing, we will need to raise additional cash and working capital to cover an expected shortfall in our cash and working capital until such time, if any, as we become cash-flow positive. We currently do not have any binding commitments for, or readily available sources of, additional financing. Should we determine it to be necessary to raise additional cash in the future as our current cash and working capital resources are depleted, we will seek to raise it through the public or private sales of debt or equity securities, the procurement of advances on contracts or licenses, funding from joint-venture or strategic partners, debt financing or short-term loans, or a combination of the foregoing. We may also seek to satisfy indebtedness without any cash outlay through the private issuance of debt or equity securities. We cannot give you any assurance that we will be able to secure the additional cash or working capital we may require to continue our operations.

***Even if we are able to raise additional financing, we might not be able to obtain it on terms that are not unduly expensive or burdensome to the company or disadvantageous to our existing shareholders.***

Even if we are able to raise additional cash or working capital through the public or private sale of debt or equity securities, the procurement of advances on contracts or licenses, funding from joint-venture or strategic partners, debt financing or short-term loans, or the satisfaction of indebtedness without any cash outlay through the private issuance of debt or equity securities, the terms of such transactions may be unduly expensive or burdensome to the company or disadvantageous to our existing shareholders. For example, we may be forced to sell or issue our securities at significant discounts to market, or pursuant to onerous terms and conditions, including the issuance of preferred stock with disadvantageous dividend, voting or veto, board membership, conversion, redemption or liquidation provisions; the issuance of convertible debt with disadvantageous interest rates and conversion features; the issuance of warrants with cashless exercise features; the issuance of securities with anti-dilution provisions; and the grant of registration rights with significant penalties for the failure to quickly register. If we raise debt financing, we may be required to secure the financing with all of our business assets, which could be sold or retained by the creditor should we default in our payment obligations. We also might be required to sell or license our products or technologies under disadvantageous circumstances we would not otherwise consider, including granting licenses with low royalty rates and exclusivity provisions.

***Our products are highly regulated. We will not be able to introduce our products to market if we cannot obtain the necessary regulatory approvals. If we are unable to obtain regulatory approvals for our products in selected key markets at all or in a timely manner, we will not be able to grow as quickly as expected, and the loss of anticipated revenues will also reduce our ability to fully fund our operations and to otherwise execute our business plan. Our failure to receive the regulatory approvals in the United States would likely cause us to go out of business.***

The manufacture, sale, promotion and marketing of our heart monitoring products and other products we intend to develop are subject to regulation by the FDA and similar government regulatory bodies in other countries. As we develop or obtain new products we will be required to determine what regulatory requirements, if any, we must comply with in order to market and sell our products in the United States and worldwide. The process of obtaining regulatory approval could take years and be very costly, if approval can be obtained at all. If we fail to comply with these requirements, we could be subjected to enforcement actions such as an injunction to stop us from marketing the product at issue or a possible seizure of our assets. We intend to work diligently to assure compliance with all applicable regulations that impact our business. We can give you no assurance, however, that we will be able to obtain regulatory approval for all of our products. We also cannot assure you that additional regulations will not be enacted in the future that would be costly or difficult to satisfy.

***Because we are not diversified, we are subject to a greater risk of going out of business should our single proposed product line fail.***

The only business opportunities we are presently pursuing are the heart monitoring or ECG market and, later, using the same technology, the neurological brain scan or EEG market. Unlike many established companies that are diversified, we do not presently have other businesses, properties, investments or other income producing assets upon which we could rely upon should our single product line fail, thereby increasing the risk of our going out of business.

***Many of our customers will rely upon third party reimbursements from third party payors to cover all or a portion of the cost of our products. If third party payors do not provide reimbursement for our products, we will not be able to grow as quickly as expected, and the loss of anticipated revenues will also reduce our ability to fully fund our operations and to otherwise execute our business plan.***

We intend to sell our heart monitoring products to individual patients and doctors, hospitals and clinics who will seek reimbursement from various third party payers, including government health programs, private health insurance plans, managed care organizations and other similar programs. We can give you no assurance that reimbursement will be available from third party payers at all, or for more than a nominal portion of the cost of our products.

***We intend to rely upon licensees, strategic partners or third party marketing and distribution partners to provide a significant part of our marketing and sales functions. Should these outside parties fail to perform as expected, we will need to develop or procure other marketing and distribution channels, which would cause delays or interruptions in our product supply and result in the loss of significant sales or customers.***

We currently have no internal sales, marketing and distribution capabilities, and will rely extensively on third-party licensees, strategic partners or third party marketing and distribution companies to perform a significant part of those functions. As a consequence of that reliance, our ability to effectively market and distribute our products will be dependent in large part on the strength and financial condition of others, the expertise and relationships of those third-parties with customers, and the interest of those parties in selling and marketing our products. Prospective third-party licensees, strategic partners and marketing and distribution parties may also market and distribute the products of other companies. If our relationships with any third-party licensees, strategic partners or marketing and distribution partners were to terminate, we would need to either develop alternative relationships or develop our own internal sales and marketing forces to continue to sell our products. Even if we are able to develop our internal sales, marketing and distribution capabilities, these efforts would require significant cash and other resources that would be diverted from other uses, if available at all, and could cause delays or interruptions in our product supply to customers, which could result in the loss of significant sales or customers. We can give you no assurance that we will be successful in our efforts to engage licensees, strategic partners or third party marketing and distribution companies to meet our sales, marketing and distribution requirements.

***We intend to rely upon the third-party FDA-approved manufacturers or suppliers to manufacture our heart monitoring products. Should these manufacturers fail to perform as expected, we will need to develop or procure other manufacturing sources, which would cause delays or interruptions in our product supply and result in the loss of significant sales and customers.***

We currently have no internal manufacturing capability, and will rely extensively on FDA-approved licensees, strategic partners or third party contract manufacturers or suppliers. Should we be forced to manufacture our products, we cannot give you any assurance that we will be able to develop an internal manufacturing capability or procure third party suppliers. Moreover, we cannot give you any assurance that any contract manufacturers or suppliers we procure will be able to supply our product in a timely or cost effective manner or in accordance with applicable regulatory requirements or our specifications.

***We are dependent for our success on a few key executive officers. Were we to lose one or more of these key executive officers, we would be forced to expend significant time and money in the pursuit of a replacement, which would result in both a delay in the implementation of our business plan and the diversion of working capital.***

Our success depends to a critical extent on the continued efforts of services of our executive management team comprised of Dr. Lowell T. Harmison, our Chief Executive Officer, Mr. Rodney Hildebrandt, our Chief Operating Officer, and Dr. Budimir S. Drakulic, our Vice President and Chief Technology Officer. Were we to lose one or more of these key executive officers, we would be forced to expend significant time and money in the pursuit of a replacement, which would result in both a delay in the implementation of our business plan and the diversion of

working capital. Messrs. Harmison and Hildebrandt are currently employed on an at-will basis, although we are in discussions relating to their entering into employment agreements. Dr. Drakulic is employed as a consultant under a loan-out agreement through October 15, 2012. None of these agreements will preclude any of these key officers from leaving the company. We currently maintain key man life insurance policies in the amount $3 million with respect to Dr. Drakulic which will assist us in recouping some of our costs in the event of the death of that officer.

***Our inability to protect our intellectual property rights could allow competitors to use our property rights and technologies in competition against our company, which would reduce our sales. In such an event we would not be able to grow as quickly as expected, and the loss of anticipated revenues will also reduce our ability to fully fund our operations and to otherwise execute our business plan.***

We rely on a combination of patent, patent pending, copyright, trademark and trade secret laws, proprietary rights agreements and non-disclosure agreements to protect our intellectual properties. We cannot give you any assurance that these measures will prove to be effective in protecting our intellectual properties. We also cannot give you any assurance that our existing patents will not be invalidated, that any patents that we currently or prospectively apply for will be granted, or that any of these patents will ultimately provide significant commercial benefits. Further, competing companies may circumvent any patents that we may hold by developing products which closely emulate but do not infringe our patents. While we intend to seek patent protection for our products in selected foreign countries, those patents may not receive the same degree of protection as they would in the United States. We can give you no assurance that we will be able to successfully defend our patents and proprietary rights in any action we may file for patent infringement. Similarly, we can give you any assurance that we will not be required to defend against litigation involving the patents or proprietary rights of others, or that we will be able to obtain licenses for these rights. Legal and accounting costs relating to prosecuting or defending patent infringement litigation may be substantial.

We also rely on proprietary designs, technologies, processes and know-how not eligible for patent protection. We cannot give you any assurance that our competitors will not independently develop the same or superior designs, technologies, processes and know-how.

While we have and will continue to enter into proprietary rights agreements with our employees and third parties giving us proprietary rights to certain technology developed by those employees or parties while engaged by our company, we can give you no assurance that courts of competent jurisdiction will enforce those agreements.

**Risks Relating To An Investment In Our Securities**

***Our common shares are sporadically or thinly traded, so you may be unable to sell at or near ask prices or at all if you need to sell your shares to raise money or otherwise desire to liquidate your shares***

Our common shares have historically been sporadically or thinly traded on the OTCBB, meaning that the number of persons interested in purchasing our common shares at or near ask prices at any given time may be relatively small or non-existent. This situation is attributable to a number of factors, including the fact that we are a small company which is relatively unknown to stock analysts, stock brokers, institutional investors and others in the investment community that generate or influence sales volume, and that even if we came to the attention of such persons, they tend to be risk-averse and would be reluctant to follow an unproven development stage company such as ours or purchase or recommend the purchase of our shares until such time as we became more seasoned and viable. As a consequence, there may be periods of several days or more when trading activity in our shares is minimal or non-existent, as compared to a seasoned issuer which has a large and steady volume of trading activity that will generally support continuous sales without a material reduction in share price. We cannot give you any assurance that a broader or more active public trading market for our common shares will develop or be sustained, or that current trading levels will be sustained. Due to these conditions, we can give you no assurance that you will be able to sell your shares at or near ask prices or at all if you need money or otherwise desire to liquidate your shares.

***The market price for our common shares is particularly volatile given our status as a relatively unknown development stage company with a small and thinly-traded public float, limited operating history and lack of revenues or profits to date for our newly introduced products, which could lead to wide fluctuations in our share price. The price at which you purchase our common shares may not be indicative of the price that will prevail in the trading market. You may be unable to sell your common shares at or above your purchase price, which may result in substantial losses to you. The volatility in our common share price may subject us to securities litigation.***

The market for our common shares is characterized by significant price volatility when compared to seasoned issuers, and we expect that our share price will continue to be more volatile than a seasoned issuer for the indefinite future. The volatility in our share price is attributable to a number of factors. First, we have relatively few common shares outstanding in the public float since most of our shares are held by a small number of shareholders. In addition, as noted above, our common shares are sporadically or thinly traded. As a consequence of this lack of liquidity, the trading of relatively small quantities of shares by our shareholders may disproportionately influence the price of those shares in either direction. The price for our shares could, for example, decline precipitously in the event that a large number of our common shares are sold on the market without commensurate demand, as compared to a seasoned issuer which could better absorb those sales without a material reduction in share price. Secondly, we are a speculative or risky investment due to our limited operating history and lack of revenues or profits to date, and uncertainty of future market acceptance for our products. As a consequence of this enhanced risk, more risk-adverse investors may, under the fear of losing all or most of their investment in the event of negative news or lack of progress, be more inclined to sell their shares on the market more quickly and at greater discounts than would be the case with the stock of a seasoned issuer. Additionally, in the past, plaintiffs have often initiated securities class action litigation against a company following periods of volatility in the market price of its securities. We may in the future be the target of similar litigation. Securities litigation could result in substantial costs and liabilities and could divert management s attention and resources.

The following factors may add to the volatility in the price of our common shares: actual or anticipated variations in our quarterly or annual operating results; acceptance of our products and services as viable security and technology solutions; government regulations, announcements of significant acquisitions, strategic partnerships or joint ventures; our capital commitments; and additions or departures of our key personnel. Many of these factors are beyond our control and may decrease the market price of our common shares, regardless of our operating performance. We cannot make any predictions or projections as to what the prevailing market price for our common shares will be at any time, including as to whether our common shares will sustain their current market prices, or as to what effect that the sale of shares or the availability of common shares for sale at any time will have on the prevailing market price.

***Since a single shareholder currently beneficially owns the majority of our outstanding common shares, that single shareholder will retain the ability to control our management and the outcome of corporate actions requiring shareholder approval notwithstanding the overall opposition of our other shareholders. This concentration of ownership could discourage or prevent a potential takeover of our company that might otherwise result in you receiving a premium over the market price for your common shares.***

ARC Finance Group, LLC, which is owned and controlled by Ms. Tracey Hampton, owns 65.4% of our outstanding common shares. As a consequence of its controlling stock ownership position, ARC Finance Group retains the ability to elect a majority of our board of directors or to remove any director, and thereby controls our management. ARC Finance Group also has the ability to control the outcome of corporate actions requiring shareholder approval, including mergers and other changes of corporate control, going private transactions, and other extraordinary transactions. ARC Finance actively evaluates potential modifications to our board of directors and management, and could make such modifications or wholesale changes at any time if deemed to be in the company's best interest.

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***The sale of a large amount of common shares held by our majority shareholder or our executive officers or directors, or the perception that such sales could occur, could substantially depress the prevailing market prices for our shares.***

The ability of our majority shareholder, ARC Finance Group, LLC, to sell common shares under Rule 144 is unclear under current SEC interpretations relating to eligibility for use of that safe harbor. As a consequence, we intend to register some or all of the common shares held by ARC Finance Group for resale to provide it with a mechanism to sell such shares on the public market in the future should it decide to do so. Some of our executive officers and directors also hold large amounts of common shares that they may sell under Rule 144 subject to control stock volume limitations. We intend to register these shares under a resale prospectus contained in a registration statement on form S-8, which would increase the overall number of such shares that those officers and directors may sell on the public markets subject to volume restrictions imposed under form S-8. Some of our executive officers and directors also hold common stock purchase options entitling them to acquire large amounts of common shares. We also intend to register these shares under a resale prospectus contained in a registration statement on form S-8, which would provide those officers and directors with a mechanism to immediately sell such shares on the public markets subject to volume restrictions imposed under form S-8.

***A large number of common shares are issuable upon conversion of our series A preferred shares or the exercise of outstanding common share purchase options or warrants. The conversion or exercise of these securities could result in the substantial dilution of your investment in terms of your percentage ownership in the company as well as the book value of your common shares. The sale of a large amount of common shares received upon the conversion or exercise of these securities on the public market to finance the exercise price or to pay associated income taxes, or the perception that such sales could occur, could substantially depress the prevailing market prices for our shares.***

There are currently outstanding as of March 25, 2005, 275,323 series A preferred shares each convertible into one common share at the conversion rate of $3 per share, and common share purchase options and warrants entitling the holders to purchase 5,060,770 common shares at a weighted average exercise price of $2.04 per share, including a number granted to directors, officers, employees and consultants that are subject to vesting conditions. In the event of the conversion or exercise of these securities, you could suffer substantial dilution of your investment in terms of your percentage ownership in the company as well as the book value of your common shares. In addition, the holders of the common share purchase options or warrants may sell common shares in tandem with their exercise of those options or warrants to finance that exercise, or may resell the shares purchased in order to cover any income tax liabilities that may arise from their conversion or exercise of these securities.

***Our issuance of additional common shares or preferred shares, or options or warrants to purchase those shares, would dilute your proportionate ownership and voting rights. Our issuance of additional preferred shares, or options or warrants to purchase those shares, could negatively impact the value of your investment in our common shares as the result of preferential voting rights or veto powers, dividend rights, disproportionate rights to appoint directors to our board, conversion rights, redemption rights and liquidation provisions granted to the preferred shareholders, including the grant of rights that could discourage or prevent the distribution of dividends to you, or prevent the sale of our assets or a potential takeover of our company that might otherwise result in you receiving a distribution or a premium over the market price for your common shares.***

We are entitled under our certificate of incorporation to issue up to 100,000,000 common and 10,000,000 blank check preferred shares. After taking into consideration our outstanding common and preferred shares as of March 25, 2005, we will be entitled to issue up to 64,918,361 additional common shares and 9,728,369 additional preferred shares. Our board may generally issue those common and preferred shares, or options or warrants to purchase those shares, without further approval by our shareholders based upon such factors as our board of directors may deem relevant at that time. Any preferred shares we may issues shall have such rights, preferences, privileges and restrictions as may be designated from time-to-time by our board, including preferential dividend rights, voting rights, conversion rights, redemption rights and liquidation provisions.  It is likely that we will be required to issue a large amount of additional securities to raise capital to further our development and marketing plans. It is also likely that we will be required to issue a large amount of additional securities to directors, officers, employees and consultants as compensatory grants in connection with their services, both in the form of stand-alone grants or under our various stock plans. We cannot give you any assurance that we will not issue additional common or preferred shares, or options or warrants to purchase those shares, under circumstances we may deem appropriate at the time.

**LEGAL PROCEEDINGS**

As of the date of this report, there are no material pending legal or governmental proceedings relating to our company or properties to which we are a party, and to our knowledge there are no material proceedings to which any of our directors, executive officers or affiliates are a party adverse to us or which have a material interest adverse to us, other than the following:

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On May 19, 2004, a complaint was filed against Recom in the Superior Court of Arizona, County of Maricopa, in an action entitled *William A. Miller v. Recom Managed Systems*. The complaint seeks declaratory relief, specific performance or damages for breach of contract. Mr. Miller alleged he was granted options to purchase 300,000 common shares of Recom at $0.01 per share. Recom believes the claim is without merit and plans to vigorously defend itself in the action. Prior to the filing of the complaint, none of the officers or directors of Recom had ever met with or spoken to Mr. Miller or his agents or even knew who Mr. Miller was. In July 2004, Recom filed a motion to dismiss the action on the basis of lack of personal jurisdiction, and is waiting for the court to set a hearing date for the motion.

**SUBMISSION OF MATTERS TO A VOTE OF SECURITIES HOLDERS**

No matters were submitted to a vote of our security holders during our fourth quarter ended December 31, 2004.

**MARKET PRICE OF AND DIVIDENDS ON OUR COMMON SHARES AND RELATED STOCKHOLDER MATTERS**

**Description Of Market**

Our common shares are currently quoted on the OTCBB under the symbol RECM. The following table sets forth the quarterly high and low bid prices for our common shares on the OTCBB for the periods indicated. The prices set forth below represent inter-dealer quotations, without retail markup, markdown or commission and may not be reflective of actual transactions. The prices have been adjusted to reflect a 3 for 1 stock split that was effective on April 11, 2003.

| | | Bid Price | |
|---|---|---|---|
| **Period** | **Volume** | **High** | **Low** |

**2004:**

| | | | |
|---|---|---|---|
| Fourth Quarter | 8,279,376 | $ 5.25 | $ 1.80 |
| Third Quarter | 6,462,439 | 4.90 | 1.93 |
| Second Quarter | 6,265,699 | 8.90 | 4.07 |
| First Quarter | 5,541,962 | 6.15 | 3.05 |

| | | | |
|---|---|---|---|
| **2003:** | | | |
| Fourth Quarter | 3,808,295 | $ 5.15 | $ 2.70 |
| Third Quarter | 3,683,800 | 5.55 | 3.24 |
| Second Quarter | 2,494,700 | 4.20 | 1.98 |
| First Quarter | 1,464,600 | 2.30 | 0.88 |

The closing price for our common shares on March 25, 2005 as reported on the OTCBB was $3.27 per share. There were 406 registered holders or persons otherwise entitled to hold our common shares as of that date pursuant to a shareholders list provided by our transfer agent as of that date and our records relating to issuable shares. The number of registered shareholders excludes any estimate by us of the number of beneficial owners of common shares held in street name.

**Dividend Policy And Restrictions On Payment Of Dividends**

We have never paid any cash dividends on our common shares, and we do not anticipate that we will pay any dividends with respect to those securities in the foreseeable future. Our current business plan is to retain any future earnings to finance the expansion development of our business. Any future determination to pay cash dividends will be at the discretion of our board of directors, and will be dependent upon our financial condition, results of operations, capital requirements and other factors as our board may deem relevant at that time.

We are prohibited from declaring any cash dividends with respect to our common shares or any other securities other than our series A preferred shares without the consent of a majority of the outstanding series A preferred shares.

**Repurchases Of Equity Securities**

During the three months ended December 31, 2004, we did not repurchase any equity securities.

**Recent Sales Of Unregistered Securities**

We have not sold or issued any securities not registered under the Securities Act of 1933 during fiscal 2004 that were not previously reported in a periodic report on form 10-QSB or on a current report on form 8-K.

**PRINCIPAL ACCOUNTANT FEES AND SERVICES**

Summarized below is the aggregate amount of various professional fees billed by our principal accountants with respect to our last two fiscal years:

| | **2004** | **2003** |
|---|---|---|
| Audit fees | $ 190,000 | $ 121,000 |
| Audit-related fees | $ | $ |

| | | |
|---|---|---|
| Tax fees | $ | $ |
| All other fees | $ | $ |
| All other fees, including tax consultation and preparation | $ | $ |

All audit fees are approved in advance by our audit committee and board of directors. Stonefield Josephson does not provide any non-audit services to Recom.

## CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

On December 1, 2003, we dismissed our independent auditor, Burnett + Company, LLC, and on December 2, 2003, we engaged Stonefield Josephson, Inc. as our independent auditor for the fiscal year ending December 31, 2003. The decision to dismiss Burnett + Company was approved by our board of directors.

Burnett + Company s reports on our financial statements as of and for the years ended December 31, 2002 and December 31, 2001 did not contain an adverse opinion or a disclaimer of opinion, nor were they modified as to uncertainty, audit scope, or accounting principles. During the periods ended December 31, 2001 and December 31, 2002, and the interim period from January 1, 2003 through the date of Burnett + Company s dismissal, we did not have any disagreements with Burnett + Company on any matter of accounting principles or practices, financial statement disclosure, or auditing scope or procedure, which disagreements, if not resolved to Burnett + Company s satisfaction, would have caused it to make a reference to the subject matter of the disagreements in connection with its reports.

Prior to engaging Stonefield Josephson, we did not consult with Stonefield Josephson regarding the application of accounting principles to a specified completed or contemplated transaction or the type of audit opinion that might be rendered on our financial statements.

## CONTROLS AND PROCEDURES

### Evaluation Of Disclosure Controls And Procedures

Disclosure controls and procedures are designed to ensure that information required to be disclosed in the reports filed or submitted under the Exchange Act is recorded, processed, summarized and reported, within the time period specified in the SEC s rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed in the reports filed under the Exchange Act is accumulated and communicated to management, including our President and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure. Our Chief Executive Officer and Chief Financial Officer, in consultation with our other members of management and advisors as appropriate, carried out an evaluation of the effectiveness of our disclosure controls and procedures as of the end of the period covered by this annual report pursuant to Rule 15d-15(b) promulgated under the Exchange Act. Based upon that evaluation, our Chief Executive Officer and our Chief Financial Officer concluded that our disclosure controls and procedures are not effective in alerting them in a timely fashion to all material information required to be included in our periodic filings with the SEC as a result of the significant deficiency described below in that subsection captioned *Significant Deficiencies In Disclosure Controls And Procedures Or Internal Controls* .

### Changes in Internal Control over Financial Reporting

The term i*nternal control over financial reporting* is defined as a process designed by, or under the supervision of, our President and Principal Financial Officer, and effected by our board of directors, management and other personnel, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. Except as noted below in that subsection captioned *Significant Deficiencies In Disclosure Controls And Procedures Or Internal Controls*, there were no changes in our internal control over financial reporting identified in connection with our evaluation of these controls as of the end of the period covered by this annual report that could have significantly affected those controls subsequent to the date of the evaluation referred to in the previous paragraph, including any correction action with regard to significant deficiencies and material weakness.

**Significant Deficiencies In Disclosure Controls And Procedures Or Internal Controls**

Our independent auditors identified that our accounting for the beneficial conversion feature of a convertible promissory note issued on December 28, 2004, which feature we had originally recognized and amortized commencing February 14, 2005 based upon management s interpretation of the application of existing accounting principles to the underlying contract documents, should have instead been recognized and amortized commencing December 28, 2004. Our independent auditors discussed this matter with our Chief Financial Officer and other members of management, and we subsequently reevaluated the transaction and recorded an adjustment. The auditors believe that this adjustment reflected a significant deficiency in our internal controls over the application of existing accounting principles to new transactions and financial reporting. This deficiency would have resulted in a material misstatement to the financial statements for the year ended December 31, 2004. We have since taken corrective action to enhance our internal controls as they relate to addressing complex accounting issues by resolving to forward our proposed treatment of these complex accounting issues to outside professionals (other than our independent auditors) for review in situations where the accounting treatment is unclear or extremely complex. We believe that the significant deficiency has been resolved.

**Other Observations**

In connection with the audit of Recom s financial statements for the year ended December 31, 2004, our independent auditors also made several other observations relating to our disclosure controls and procedures or internal controls. First, our independent auditors observed that Recom did not have adequate segregation of duties due to the size of the company, and that management had the ability to override any existing controls. Management acknowledges the existence of this problem, and is developing procedures to address them to the extent possible given the acknowledged limitations. Secondly, our independent auditors observed that Recom did not have a comprehensive accounting procedures manual including information as to customized internal control structure, documentation and transaction flow. Our management acknowledges the existence of this problem, and is developing procedures to address them to the extent possible given limitations in financial and manpower resources. Finally, our independent auditors observed that none of the members of our audit committee demonstrated an in-depth understanding of generally accepted accounting principles. We acknowledge that while we believe our audit committee members are proficient in reading and understanding financial statements, they may not have an in-depth understanding of generally accepted accounting principles, and we are currently evaluating whether we should seek a person with a professional accounting background to join the board and to serve on the audit committee.

**OTHER INFORMATION**

During the fourth quarter of fiscal 2004, there was no information required to be disclosed in a report on form 8-K that was not reported.

**EXHIBITS**

2.1

Order dated October 26, 2000 Confirming Plan of Reorganization and Granting Final Approval of Disclosure Statement (9)

3.1

Amended And Restated Certificate Of Incorporation Of Recom Managed System, Inc. filed by the Delaware Secretary of State on November 6, 2000 (1)

3.2

Certificate Of Amendment Of Certificate Of Incorporation Of Recom Managed System, Inc. filed by the Delaware Secretary of State on June 20, 2003 (8)

3.3

Certificate Of Designation Of Rights, Preferences And Limitations Of Series A Convertible Preferred Stock Of Recom Managed System, Inc. filed by the Delaware Secretary of State on September 9, 2003 (9)

3.4

Amendment To Certificate Of Designation Of Rights, Preferences And Limitations Of Series A Convertible Preferred Stock Of Recom Managed System, Inc. filed by the Delaware Secretary of State on April 26, 2004 (9)

3.5

Bylaws Of Recom Managed Systems, Inc. adopted March 31, 2003 (6)

5.1

Specimen common stock certificate (8)

5.2

Specimen series A preferred stock certificate (8)

5.3

Recom Managed Systems, Inc. 2002 Stock Plan adopted on November 1, 2002 (6)

5.4

Form of option issued under Recom Managed Systems, Inc. 2002 Stock (8)

5.5

Recom Managed Systems, Inc. 2003 Nonqualified Stock Option And Stock Plan adopted on March 31, 2002 (6)

5.6

Warrant To Purchase Common Stock dated September 19, 2002 issued to Sim Farrar (2)

5.7

Form of Standard Warrant (8)

5.8

Form of Class A Warrant (8)

5.9

Form of Class C Warrant (8)

5.10

Agent s Warrant dated November 1, 2003 with Maxim Group LLC (9)

5.11

Agent s Warrant dated November 1, 2003 with Jenkins Capital Management, LLC (11)

10.1

Standard Multi-Tenant Office Lease dated August 20, 2002 between Bershin Properties I, LLC, as lessor, and Recom Managed Systems, Inc., LLC, as lessee (9)

10.2

Addendum To Standard Office Lease dated August 20, 2002 between Bershin Properties I, LLC, as lessor, and Recom Managed Systems, Inc., as lessee (9)

10.3

Addendum To Standard Office Lease dated December 17, 2003 between Bershin Properties I, LLC, as lessor, and Recom Managed Systems, Inc., as lessee (9)

10.4

Stock Acquisition and Signal Technologies Transfer Agreement dated September 12, 2002 between Recom Managed Systems, Inc. and ARC Finance Group, LLC (2)

10.5

Employment Agreement dated October 14, 2002 between Recom Managed Systems, Inc. and Marvin H. Fink (3)

10.6

License Agreement dated December 9, 1993 between Dr. Budimir S. Drakulic and Teledyne Electronic Industries, Inc. (8)

10.7

Restricted Stock Agreement dated October 14, 2002 between Recom Managed Systems, Inc. and Marvin H. Fink (3)(4)

10.8

Indemnification Agreement dated October 14, 2002 between Recom Managed Systems, Inc. and Marvin H. Fink (3)(4)

10.9

Loan-out Agreement dated October 15, 2002 between Recom Managed Systems, Inc. and Budimir Drakulic, B World and B Technologies (3)

10.10

Restricted Stock Agreement dated October 15, 2002 between Recom Managed Systems, Inc. and Budimir Drakulic, B World and B Technologies (3)(5)

10.11

Consulting Agreement dated November 1, 2002 between Recom Managed Systems, Inc. and Ellsworth Roston (3)

10.12

Employment, Confidential Information, Invention Assignment, And Arbitration Agreement dated October 15, 2002 between Recom Managed Systems, Inc. and Budimir Drakulic, B World and B Technologies (3)(5)

10.13

Consulting Agreement dated February 14, 2003 between Recom Managed Systems, Inc. and Lowell T. Harmison (8)

10.14

Employment Agreement dated March 10, 2003 between Recom Managed Systems, Inc. and Charles E. McGill (6)

10.15

Investment Banking Agreement dated April 15, 2003 between Recom Managed Systems, Inc. and Brookstreet Securities Corporation (7)

10.16

Investment Banking Agreement dated July 17, 2003 between Recom Managed Systems, Inc. and Maxim Group, LLC (9)

10.17

Placement Agency Agreement dated September 4, 2003 between Recom Managed Systems, Inc. and Maxim Group, LLC (9)

10.18

Form of Registration Rights Agreement for purchasers of Series A Preferred Stock (8)

10.19

Scope Letters and Engagement Agreements dated December 18, 2003, January 23, 2004 and March 22, 2004 between Recom Managed Systems, Inc. and CFO 911 (9)

10.20

Non-Binding Letter of Intent dated January 10, 2004 between Recom Managed Systems, Inc. and TZ Medical Inc. (9)

10.21

Settlement Agreement And Releases, Warrant and Piggyback Registration Rights Agreement each dated April 28, 2004 between Recom Managed Systems, Inc., Mitchell J. Stein, ARC Finance Group, LLC, Tracey Hampton-Stein and Rex Julian Beaber (9)

10.22

Consulting Agreement between Recom Managed Systems, Inc. and Dr. Michael Laks (10)

10.23

Consulting Agreement between Recom Managed Systems, Inc. and Dr. Mitchell W. Krucoff (10)

10.24

Research And Development Services Agreement dated May 12, 2004 between Recom Managed Systems, Inc. and Battelle Memorial Institute (10)

10.25

Consulting Agreement between Recom Managed Systems, Inc. and Dr. Andrea Natale (11)

10.26

Sponsored Research Agreement dated August 30, 2004 between Recom Managed Systems, Inc. and Duke Clinical Research Institute (12)

10.27

Securities Purchase Agreement dated December 29, 2004 between Recom Managed Systems, Inc. and DKR SoundShore Oasis Holding Fund Ltd. (13)

10.28

8% Convertible Debenture dated December 29, 2004 granted to DKR SoundShore Oasis Holding Fund Ltd. (13)

10.29

Common Stock Purchase Warrant dated December 29, 2004 granted to DKR SoundShore Oasis Holding Fund Ltd. (13)

10.30

Registration Rights Agreement dated December 29, 2004 between Recom Managed Systems, Inc. and DKR SoundShore Oasis Holding Fund Ltd. (13)

10.31

Consulting Agreement dated January 21, 2005 between Recom Managed Systems, Inc. and Dr. Lowell T. Harmison *

10.32

Research and Development Services Agreement with Battelle Memorial Institute dated February 3, 2005 *

21

List of subsidiaries *

23

Consent of Stonefield Josephson, Inc. *

24

Powers of Attorney for Lucy Duncan-Scheman, Rodney Hildebrandt, Ellsworth Roston, Jennifer Black and Pamela Bunes *

31.1

Certification of principal executive officer pursuant to Section 302 of the Sarbanes-Oxley Act *

31.2

Certification of principal financial officer pursuant to Section 302 of the Sarbanes-Oxley Act *

32.1

Certification of chief executive officer pursuant to Section 906 of the Sarbanes-Oxley Act *

32.2

Certification of chief financial officer pursuant to Section 906 of the Sarbanes-Oxley Act *

*

Filed herewith

(1)

Previously filed as an exhibit to our report on form 10-KSB for our fiscal year ended December 31, 2001 filed with the SEC on February 22, 2002.

(2)

Previously filed as an exhibit to our report on form 8-K filed with the SEC on September 25, 2002.

(3)

Previously filed as an exhibit to our report on form 10-QSB for our fiscal quarter ended September 30, 2002 filed with the SEC on November 12, 2002.

(4)

Filed as part of the Employment Agreement for Mr. Fink noted in item 10.5.

(5)

Filed as part of the Loan-Out Agreement for with B World Technologies, B Technologies and Dr. Drakulic noted in item 10.9.

(6)

Previously filed as an exhibit to our report on form 10-KSB for our fiscal year ended December 31, 2002 filed with the SEC on March 26, 2003.

(7)

Previously filed as an exhibit to our report on form 10-QSB for our fiscal quarter ended March 30, 2003 filed with the SEC on May 7, 2003.

(8)

Previously filed as an exhibit to our registration statement on form SB-2 filed with the SEC on January 2, 2004.

(9)

Previously filed as an exhibit to our registration statement on form SB-2 (amendment no. 2) filed with the SEC on May 11, 2004.

(10)

Previously filed as an exhibit to our registration statement on form SB-2 (amendment no. 3) filed with the SEC on July 26, 2004.

(11)

Previously filed as an exhibit to our registration statement on form SB-2 (amendment no. 4) filed with the SEC on October 18, 2004.

(12)

Previously filed as an exhibit to our registration statement on form SB-2 (amendment no. 5) filed with the SEC on November 5, 2004.

(13)

Previously filed as an exhibit to our report on form 8-K filed with the SEC on December 30, 2004.

(14)

Previously filed as an exhibit to our registration statement on form SB-2 filed with the SEC on January 26, 2005.

**RECOM MANAGED SYSTEMS, INC.**

**ANNUAL FINANCIAL STATEMENTS**

**DECEMBER 31, 2004**

## REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

**To The Board Of Directors And Stockholders Of Recom Managed Systems, Inc.**
Studio City, California

We have audited the accompanying balance sheet of Recom Managed Systems, Inc. as of December 31, 2004 and the related statements of operations, stockholders' equity and cash flows for each of the two years in the period ended December 31, 2004 and from inception of development stage (November 7, 2000) to December 31, 2004. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Recom Managed Systems, Inc. as of December 31, 2004 and the results of its operations and its cash flows for each of the two years in the period ended December 31, 2004 and from inception of development stage (November 7, 2000) to December 31, 2004, in conformity with accounting principles generally accepted in the United States of America.

The accompanying financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America, which contemplate continuation of the company as a going concern. As discussed in Note 1, the Company has incurred significant net losses since its inception, has an accumulated deficit of $14,421,842, has used cash for operating activities of $3,693,105 during the year ended December 31, 2004 and has debt of $2,000,000 maturing in increments by August 31, 2005. The Company does not anticipate introducing its first product to market until early 2006 and management has stated that it believes that the Company has sufficient capital to fund its operations only through August 2005. The foregoing matters raise substantial doubt about the ability of the Company to continue as a going concern. Management's plans in regard to these matters are also described in Note 1. These financial statements do not include any adjustments that might result from the outcome of these uncertainties.

*/s/ Stonefield Josephson, Inc.*

Stonefield Josephson, Inc.
Certified Public Accountants

March 18, 2005

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

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**RECOM MANAGED SYSTEMS, INC.**

**(A Development Stage Company)**

**BALANCE SHEET**

**December 31, 2004**

**ASSETS**

| | | |
|---|---|---|
| Current assets: | | |
| Cash and cash equivalents | $ | 2,340,806 |
| Prepaid expenses | | 236,906 |
| Total current assets | | 2,577,712 |
| Property and equipment, net of accumulated depreciation of $98,588. | | 143,606 |
| Intangible patents, net of accumulated amortization of $22,292 | | |

| | | |
|---|---|---|
| | | 330,682 |
| TOTAL ASSETS | | |
| | $ | 3,052,000 |

**LIABILITIES AND STOCKHOLDERS EQUITY**

| | | |
|---|---|---|
| Current liabilities: | | |
| Accounts payable and accrued expenses | | |
| | $ | 392,120 |
| Convertible debenture payable, net of unamortized debt discount of $873,721 | | |
| | | 1,126,279 |
| Warrants issued with registration rights | | |
| | | 578,000 |
| Total current liabilities | | |
| | | 2,096,399 |
| Commitments and contingencies | | |
| Stockholders equity: | | |
| Series A convertible preferred stock, $.001 par value; 10,000,000 shares authorized; 246,342 shares issued and outstanding | | |

| | |
|---|---|
| | 246 |
| Series A convertible preferred stock to be issued for accrued dividends, 131,377 shares | |
| | 131 |
| Common stock, $.001 par value;<br>100,000,000 shares authorized; 34,826,655 shares issued and outstanding | |
| | 34,827 |
| Additional paid-in capital | |
| | 15,348,728 |
| Deferred equity-based expense | |
| | (6,489) |
| Deficit accumulated during development stage | |
| | (14,421,842) |
| Total stockholders equity | |
| | 955,601 |
| TOTAL LIABILITIES AND STOCKHOLDERS EQUITY | |
| | $ 3,052,000 |

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

**RECOM MANAGED SYSTEMS, INC.**

**(A Development Stage Company)**

**STATEMENTS OF OPERATIONS**

**For The Years Ended December 31, 2004 And 2003 And From Inception**

**Of Development Stage (November 7, 2000) To December 31, 2004**

| | For the Years Ended December 31, | | From Inception of Development Stage (Nov. 7, 2000) to Dec. 31, 2004 |
|---|---|---|---|
| | 2004 | 2003 | |
| Revenue | | | $ |

$

$

Research and development

1,663,362

497,631

2,228,493

General and administrative expenses

5,052,580

4,818,443

10,102,150

Loss before other income (expense)

(6,715,942)

(5,316,074)

(12,330,643)

Interest income

| | |
|---|---|
| | 53,820 |
| | 4,697 |
| | 58,517 |
| Interest expense | |
| | (15,175) |
| | (15,175) |
| Warrant repricing and other | |
| | (288,946) |
| | (288,946) |
| Loss before provision for income taxes | |
| | (6,966,243) |
| | (5,311,377) |
| | (12,576,247) |

| | | | |
|---|---|---|---|
| Provision for income taxes | | | |
| Net loss | (6,966,243) | (5,311,377) | (12,576,247) |
| Preferred dividend | 295,452 | 1,953,170 | 2,248,622 |
| Net loss attributable to common stockholders | $ (7,261,695) | $ (7,264,547) | |

| | | |
|---|---|---|
| | $ | (14,824,869) |
| Basic and diluted loss per share | | |
| | $ | (0.21) |
| | $ | (0.17) |
| | $ | (0.64) |
| Basic and diluted loss per share attributable to common stockholders | | |
| | $ | (0.22) |
| | $ | (0.23) |
| | $ | (0.75) |
| Weighted average shares outstanding basic and diluted | | |
| | | 33,632,117 |
| | | 31,765,404 |
| | | 19,736,701 |

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

**RECOM MANAGED SYSTEMS, INC.**

**(A Development Stage Company)**

**STATEMENTS OF STOCKHOLDERS EQUITY**

**From Inception Of Development Stage (November 7, 2000) To December 31, 2004**

**Common Stock**

**Series A Convertible Preferred Stock**

**Series A Convertible Preferred Stock To Be Issued**

**Additional Paid-in Capital**

**Deferred Compen- sation**

**Deficit Accumu- lated During Develop- ment Stage**

**From Inception (Nov. 7, 2000) To Dec. 31, 2004**

**Shares**

**Amount**

**Shares**

**Amount**

**Shares**

**Amount**

**2000:**

Balance November 7, 2000 (as restated for 3:1 stock split)

4,139,784

$ 4,139

$

$

$ (4,139)

$

$

$

Contributed capital

35,000

35,000

Net loss

(36,673)

(36,673)

Balance December 31, 2000

4,139,784

4,139

30,861

(36,673)

(1,673)

**2001:**

Capital contributed

45,000

45,000

Shares issued for services July 2001 $0.033

150,000

150

4,850

5,000

Net loss

(50,000)

(50,000)

Balance December 31, 2001

4,289,784

4,289

80,711

(86,673)

(1,673)

**2002:**

Capital contributed

56,400

56,400

Warrants issued for cash

305

125,000

125,000

Issuance of common stock for:

| | | | |
|---|---|---|---|
| Technology | Sept. 2002 | $0.006 | |
| | | | 23,400,000 |
| | | | 23,400 |
| | | | 54,623 |

78,023

Services rendered Oct. 2002 $0.021

2,925,000

2,925

17,958

(19,678)

1,205

Cash Oct 2002 $0.03

564,810

565

17,221

17,786

| | | | |
|---|---|---|---|
| Cash | Nov 2002 | $2.66 | |
| | | | 71,250 |
| | | | 71 |
| | | | 189,929 |
| | | | 190,000 |
| Contributed services officer | | | |

20,000

20,000

Warrants issued for services

5,324

5,324

Net loss

-

-

(211,954)

(211,954)

Balance December 31, 2002

31,250,844

31,250

567,166

(19,678)

(298,627)

280,111

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

**RECOM MANAGED SYSTEMS, INC.**

**(A Development Stage Company)**

**STATEMENTS OF STOCKHOLDERS EQUITY**

**From Inception Of Development Stage (November 7, 2000) To December 31, 2004**

**2003:**

Issuance of common stock for cash and contributed property April 2003 $2.22

112,812

113

249,887

250,000

Issuance of common stock for cash:

May 2003 $3.00

82,667

83

247,917

248,000

May 2003 $3.33

75,075

75

249,925

250,000

Issuance of common stock for services:

April 2003 $2.80

147,192

147

411,654

411,801

April 2003 $3.15

11,045

11

34,780

34,791

July 2003 $3.67

111,625

112

410,192

410,304

August 2003 $3.68

33,188

33

121,103

121,136

September 2003 $3.77

24,292

24

91,673

91,697

October 2003 $4.78

15,385

15

73,525

73,540

November 2003 $3.65

18,834

19

68,783

68,802

December 2003 $3.60

5,953

6

21,425

21,431

Cashless exercise of warrants

1,105,000

1,105

(1,105)

Contributed services officer

80,000

80,000

Employee stock options issued below market

38,400

38,400

Amortization of deferred compensation

6,668

6,668

Options and warrants issued for:

Services

2,196,068

(219,010)

1,977,058

Financing cost

74,088

74,088

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

**RECOM MANAGED SYSTEMS, INC.**

**(A Development Stage Company)**

**STATEMENTS OF STOCKHOLDERS EQUITY**

**From Inception Of Development Stage (November 7, 2000) To December 31, 2004**

| | |
|---|---|
| Issuance of preferred stock for cash | |
| | 1,792,975 |
| | 1,793 |

5,376,857

5,378,650

Series A preferred stock offering expenses

(572,785)

(572,785)

Preferred stock beneficial conversion feature

896,474

(896,474)

Allocation of fair value to warrants

949,121

(949,121)

Series A Preferred stock accrued dividend

(107,575)

(107,575)

Net loss

(5,311,377)

(5,311,377)

Balance December 31, 2003

32,993,912

$ 32,993

1,792,975

$ 1,793

$ 11,477,573

$ (232,020)

$ (7,455,599)

$ 3,824,740

**2004:**

Issuance of common stock for services:

January 2004 $3.63

52,391

52

190,088

190,140

February 2004 $4.24

25,714

26

108,979

109,005

March 2004 $4.90

47,638

48

233,584

233,632

April 2004 $7.39

11,937

12

88,145

88,157

May 2004 $6.66

43,425

43

289,006

289,049

June 2004 $4.30

16,976

17

72,980

72,997

July 2004 $3.90

21,583

22

84,206

84,228

August 2004 $3.56

26,885

27

95,570

95,597

September 2004 $3.67

49,035

49

179,738

179,787

October 2004 $2.67

55,420

55

148,163

148,218

November 2004 $2.94

32,635

33

95,914

95,947

December 2004 $4.52

69,504

70

313,947

314,017

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

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**RECOM MANAGED SYSTEMS, INC.**

**(A Development Stage Company)**

**STATEMENTS OF STOCKHOLDERS EQUITY**

**From Inception Of Development Stage (November 7, 2000) To December 31, 2004**

| | |
|---|---|
| Exercise of class A warrants for cash | |
| | 130,030 |
| | 130 |

274,870

275,000

Exercise of class C warrants for cash

16,665

17

49,979

49,996

Cashless exercise of warrants

51,815

52

(52)

| | |
|---|---|
| Contributed services officer | |
| | 80,000 |
| | 80,000 |
| Amortization of deferred compensation | |

225,531

225,531

Warrants issued for services

132,712

132,712

Warrants issued for legal settlement

757,207

757,207

Expense recognized from repricing of warrants

158,516

158,516

Beneficial conversion feature

408,333

408,333

Cancelled common stock

(369,000)

(369)

369

Conversion of series A preferred stock

1,546,633

1,547

(1,546,633)

(1,547)

Series A preferred stock accrued dividend

(295,452)

(295,452)

Shares for series A preferred dividends

134,834

134

404,353

404,487

Conversion of series A preferred stock

3,457

3

(3,457)

(3)

Net loss

| | |
|---|---|
| | (6,966,243) |
| | (6,966,243) |
| Balance December 31, 2004 | |
| | 34,826,655 |
| | $ 34,827 |
| | 246,342 |
| | $ 246 |
| | 131,377 |
| | $ 131 |
| | $ 15,473,728 |

$ (6,489)

$ (14,121,842)

$ 955,601

.

The accompanying notes are an integral part of these financial statements

**RECOM MANAGED SYSTEMS, INC.**

**(A Development Stage Company)**

**STATEMENTS OF CASH FLOWS**

**From Inception Of Development Stage (November 7, 2000) To December 31, 2004**

| | For the Years Ended December 31, | | |
|---|---|---|---|
| | From Inception of Development Stage (Nov. 7, 2000) to Dec. 31, 2004 | 2004 | 2003 |
| CASH FLOWS FROM OPERATING ACTIVITIES: | | | |
| Net loss | $ (6,966,243) | | |

| | |
|---|---|
| | $ (5,311,377) |
| | $ (12,576,247) |
| Adjustments to reconcile net loss to net cash used in operating activities: | |
| Depreciation and amortization | |
| | 69,984 |
| | 50,897 |
| | 121,574 |
| Amortization of debt issue costs and finance costs | |
| | 144,272 |
| | 144,272 |
| Amortization of deferred compensation | |
| | 225,531 |
| | 6,668 |

233,404

Services recognized as contributed capital

80,000

80,000

180,000

Stock issued for services

1,900,774

1,383,503

3,289,276

Options and warrants issued for services

132,712

2,089,546

2,227,582

Warrants issued for legal settlement

757,207

757,207

Finance cost attributed to repricing of warrants

158,516

158,516

Other

1,459

1,459

Changes in operating assets and liabilities:

Prepaid expenses and other currents assets

(106,157)

(92,934)

(236,906)

Accounts payable and accrued expenses

(91,160)

470,517

392,122

Net cash used in operating activities

(3,693,105)

(1,323,180)

(5,307,741)

CASH FLOWS FROM INVESTING ACTIVITIES:

Purchase of property and equipment

(33,145)

(180,703)

(242,889)

Capitalized patent cost

(184,000)

(90,951)

(274,951)

Net cash used in investing activities

(217,145)

(271,654)

(517,840)

CASH FLOWS FROM FINANCING ACTIVITIES:

Capital contributions

136,400

Issuance of common stock and exercise of warrants for cash

324,996

598,000

1,130,782

Sale of preferred stock for cash, net of expenses

4,805,865

4,805,865

Sale of warrants for cash

125,000

Proceeds from issuance of convertible debenture, net of expenses

1,968,340

1,968,340

| | | | |
|---|---|---|---|
| Net cash provided by financing activities | 2,293,336 | 5,403,865 | 8,166,387 |
| Net increase (decrease) in cash and cash equivalents | (1,616,914) | 3,809,031 | 2,340,806 |
| Cash and cash equivalents, beginning of period | 3,957,720 | 148,689 | |
| Cash and cash equivalents, end of period | $ 2,340,806 | $ 3,957,720 | |

$ 2,340,806

The accompanying notes are an integral part of these financial statements

**RECOM MANAGED SYSTEMS, INC.**

**(A Development Stage Company)**

**STATEMENTS OF CASH FLOWS**

**From Inception Of Development Stage (November 7, 2000) To December 31, 2004**

**Supplemental Cash Flow Information:**

For the years from inception of development stage (November 7, 2000) to December 31, 2004, Recom paid no interest or income taxes.

**Supplemental Investing and Financing Activities:**

In September 2002, 23,400,000 shares of common stock were issued for a patent valued at $78,023.

In April 2003, Recom entered into an agreement with a major shareholder in which $150,000 of common stock was issued for $33,208 of accrued expenses and $116,792 of furniture and fixtures and leasehold improvements.

Recom recorded compensation expense of $80,000 for each of the years ended December 31, 2004 and 2003, respectively for the Chief Executive Officer of the company. This compensation was recorded as additional paid in capital.

For the years ended December 31, 2004 and 2003, Recom accrued $295,452 and $107,757, respectively, in dividends related to the series A convertible preferred stock. Such dividends are a non-cash charge as they have been or will be paid in-kind.

During 2004, Recom recorded a discount on debt related to the issuance of a convertible debenture in the amount of $855,903, resulting from a beneficial conversion feature attributable to the conversion provisions of the debenture and from a warrant issued with the debenture.

During 2004, 1,546,633 shares of common stock were issued upon conversion of an equivalent number of series A preferred stock.

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**RECOM MANAGED SYSTEMS, INC.**

**(A Development Stage Company)**

**NOTES TO FINANCIAL STATEMENTS**

**From Inception Of Development Stage (November 7, 2000) To December 31, 2004**

**1.**

**ORGANIZATIONAL MATTERS**

**Reorganization**

On June 26, 2000, Recom Managed Systems, Inc. ( *we* , *us* , *our company* or *Recom* ) (a Development Stage Compan filed a Voluntary Petition for Reorganization Under Chapter 11 of the Federal Bankruptcy Code and substantially curtained operations. The Plan of Reorganization was confirmed on November 7, 2000, at which date the company became a development stage company under the provisions of Statement of Financial Accounting Standards ("*SFAS*") No. 7. This resulted in the post bankruptcy ownership group controlling approximately 87% of the common stock and the elimination of the outstanding liabilities and most assets.

On September 19, 2002, we issued 23,400,000 (7,800,000 pre-split) shares of common stock in exchange for intangible technology. The issuance of this stock resulted in a change of control, with the new ownership group controlling approximately 85% of the company s outstanding stock (See Note 4). Recom is now developing technology in the medical device market focused on cardiac monitors and other diagnostic medical devices which monitor and measure the body s physiological signals in order to detect and prevent medical complications and diseases.

We are authorized under our Certificate of Incorporation to issue (1) common shares, par value $.001 per share, and (2) shares of preferred stock, par value $.001 per share, of which one class, denominated as series A convertible preferred stock, has been designated to date. We sometime refer to these securities in these financial statements as *common shares* , *preferred shares* and *series* A *preferred shares* , respectively.

**Nature of Business**

Recom is a development stage medical device company focused on researching, developing and marketing cardiac monitors and other diagnostic medical devices which monitor and measure physiological signals in order to detect diseases that impact an individual s health.

**Basis of Presentation**

On October 21, 2003, we formed Memonitor, Inc., a Delaware corporation, to act as a vehicle for the prospective application of our technology for the treatment and monitoring of Alzheimer s, Parkinson s and related neurological diseases of the brain. To date, Memonitor has remained a dormant corporation and has not been included in these financial statements.

**Stock Split**

On April 2, 2003, our board of directors declared a three-for-one stock split effective as of the close of business on April 11, 2003. All share amounts, exercise prices relating to share purchase options and warrants, and earnings per share referred to in these financial statements and notes are presented on a post-split basis unless stated otherwise.

**Going Concern**

The accompanying financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America, which contemplate continuation of our company as a going concern. However, we have incurred significant net losses since our inception, have an accumulated deficit of $14,421,842 as of December 31, 2004, have used cash for operating activities of $3,693,105 during the year ended December 31, 2004 and have debt of $2,000,000 maturing in increments by August 31, 2005.

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We do not anticipate introducing our first product to market until early 2006, and our management believes that we have sufficient capital to fund our operations only through August 2005 assuming the conversion of the foregoing indebtedness into common shares (see Notes 8 and 13) and further assuming that we reduce our expenditures to minimal levels and do not enter into any commitments for material expenditures. The foregoing matters raise substantial doubt about the ability of our company to continue as a going concern. These financial statements do not include any adjustments relating to the recoverability and classification of recorded asset amounts, or amounts and classification of liabilities that might be necessary should our company be unable to continue as a going concern.

In order to address our capital requirements, we intend to seek to raise additional cash for working capital purposes through the public or private sales of debt or equity securities, the procurement of advances on contracts or licenses, funding from joint-venture or strategic partners, debt financing or short-term loans, or a combination of the foregoing. We may also seek to satisfy indebtedness without any cash outlay through the private issuance of debt or equity securities. We do not currently have any binding commitments for, or readily available sources of, additional financing.

**2.**

**SIGNIFICANT ACCOUNTING POLICIES**

***Use of Estimates*** These financial statements have been prepared in accordance with accounting principles generally accepted in the United States and, accordingly, require management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Specifically, our management has estimated the expected economic life and value of our patents, our net operating loss for tax purposes and our stock, option and warrant expenses related to compensation to employees and directors, consultants and investment banks. Actual results could differ from those estimates.

***Fair Value of Financial Instruments*** For certain of our financial instruments, including accounts payable and accrued expenses and note payable, the carrying amounts approximate fair value due to their relatively short maturities.

***Cash and Equivalents*** Cash equivalents are comprised of certain highly liquid investments with maturity of three months or less when purchased. We maintain our cash in bank deposit accounts, which at times, may exceed federally insured limits. We have not experienced any losses in such account.

***Equipment*** We record our equipment at historical cost. We expense maintenance and repairs as incurred. Depreciation is provided for by the straight-line method over three to five years.

***Intangible and Long-Lived Assets*** We follow SFAS No. 144, *Accounting for Impairment of Disposal of Long-Lived Assets*, which established a primary asset approach to determine the cash flow estimation period for a group of assets and liabilities that represents the unit of accounting for a long lived asset to be held and used. Long-lived assets to be held and used are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. The carrying amount of a long-lived asset is not recoverable if it exceeds the sum of the undiscounted cash flows expected to result from the use and eventual disposition of the asset. Long-lived assets to be disposed of are reported at the lower of carrying amount or fair value less cost to sell. During the years ended December 31, 2004 and 2003, no impairment loss was recognized.

***Advertising Costs*** Advertising costs are expensed as incurred and amounted to $9,087 and $11,800 for the years ended December 31, 2004 and 2003, respectively.

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***Research and Development Costs*** Research and development costs consist of expenditures for the research and development of patents and technology, which are not capitalizable. Our research and development costs consist mainly of payroll and payroll related expenses, consultants, testing and FDA regulatory expenses.

***Stock Based Compensation*** SFAS No. 123, *Accounting for Stock-Based Compensation*, establishes and encourages the use of the fair value based method of accounting for stock-based compensation arrangements under which compensation cost is determined using the fair value of stock-based compensation determined as of the date of the grant or the date at which the performance of the services is completed and is recognized over the periods in which the related services are rendered. The statement also permits companies to elect to continue using the current intrinsic value accounting method specified in Accounting Principles Board ( *APB* ) Opinion No. 25, *Accounting for Stock Issued to Employees*, to account for stock-based compensation to employees. We have elected to use the intrinsic value based method for grants to our employees and directors and have disclosed the pro forma effect of using the fair value based method to account for our stock-based compensation to employees.

Recom uses the fair value method for equity instruments granted to non-employees and uses the Black Scholes model for measuring the fair value. The stock based fair value compensation is determined as of the date of the grant or the date at which the performance of the services is completed (measurement date) and is recognized over the periods in which the related services are rendered.

**Pro Forma Information**

***Employee and Director Common Share Purchase Options*** Pro forma information regarding the effects on operations of employee and director common share purchase options as required by SFAS No. 123 and SFAS No. 148 has been determined as if Recom had accounted for those options under the fair value method. Pro forma information is computed using the Black Scholes method at the date of grant of the options based on the following assumptions ranges: (1) risk free interest rate of 1.42% to 3.13%; (2) dividend yield of 0%; (3) volatility factor of the expected market price of our common stock of 53.84% to 158.48%; and (4) an expected life of the options of 1.5 years. The foregoing option valuation model requires input of highly subjective assumptions. Because common share purchase options granted to employees and directors have characteristics significantly different from those of traded options, and because changes in the subjective input assumptions can materially affect the fair value of estimate, the existing model does not in the opinion of our management necessarily provide a reliable single measure of fair value of common share purchase options we have granted to our employees and directors..

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Pro forma information relating to employee and director common share purchase options is as follows:

| | For the Year Ended December 31, 2004 | For the Year Ended December 31, 2003 |
|---|---|---|
| Net loss as reported | $ (6,966,243) | $ (5,311,377) |
| Current period expense calculated under APB 25 | | 38,400 |
| Stock compensation calculated under SFAS 123 | | (389,199) |

| | | |
|---|---|---|
| | | (730,865) |
| Pro forma net loss | | |
| | | $ (7,355,442) |
| | | $ (6,003,842) |
| Basic and diluted historical loss per share | | |
| | | $ (0.21) |
| | | $ (0.17) |
| Pro forma basic and diluted loss per share | | |
| | | $ (0.22) |
| | | $ (0.19) |
| Net loss attributable to common shares, as reported | | |
| | $ (7,261,695) | |
| | | $ (7,264,547) |
| Pro forma net loss attributable to common shares | | |
| | $ (7,650,894) | |

| | | |
|---|---|---|
| | $ | (7,957,012) |
| Basic and diluted historical loss per share attributable to common shares | | |
| | $ | (0.22) |
| | $ | (0.23) |
| Pro forma basic and diluted loss per share attributable to common shares | | |
| | $ | (0.23) |
| | $ | (0.25) |

***Income Taxes*** Deferred income taxes result primarily from temporary differences between financial and tax reporting. Deferred tax assets and liabilities are determined based on the difference between the financial statement bases and tax bases of assets and liabilities using enacted tax rates. A valuation allowance is recorded to reduce a deferred tax asset to that portion that is expected to more likely than not be realized.

***Net Loss Per Share*** We use SFAS No. 128, *Earnings Per Share* for calculating the basic and diluted loss per share. We compute basic loss per share by dividing net loss and net loss attributable to common shareholders by the weighted average number of common shares outstanding. Diluted loss per share is computed similar to basic loss per share except that the denominator is increased to include the number of additional common shares that would have been outstanding if the potential shares had been issued and if the additional shares were dilutive. Common equivalent shares are excluded from the computation of net loss per share if their effect is anti-dilutive.

Per share basic and diluted net loss attributable to common stockholders amounted to $0.22 for the year ended December 31, 2004 and $0.23 for the year ended December 31, 2003. For the years ended December 31, 2004 and 2003, 5,417,565 potential shares and 7,121,431 potential shares, respectively, were excluded from the shares used to calculate diluted earnings per share as their inclusion would reduce net loss per share.

***Comprehensive Income*** A statement of comprehensive income is not presented in our financial statements since we did not have any of the items of other comprehensive income in any period presented.

**New Accounting Pronouncements**

In November 2004, the FASB issued SFAS No. 151, *Inventory Costs, an amendment of ARB No. 43, Chapter 4*. The amendments made by Statement 151 clarify that abnormal amounts of idle facility expense,

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freight, handling costs, and wasted materials (spoilage) should be recognized as current period charges and require the allocation of fixed production overheads to inventory based on the normal capacity of the production facilities. The guidance is effective for inventory costs incurred during fiscal years beginning after June 15, 2005. Earlier application is permitted for inventory costs incurred during fiscal years beginning after November 23, 2004. Recom has evaluated the impact of the adoption of SFAS 151, and does not believe the impact will be significant to the company's overall results of operations or financial position since Recom currently does not have any manufacturing operations or inventory.

In December 2004, the FASB issued SFAS No.152, *Accounting for Real Estate Time-Sharing Transactions, an amendment of FASB Statements No. 66 and 67 (SFAS 152)*. The amendments made by Statement 152 amend FASB Statement No. 66, *Accounting for Sales of Real Estate*, to reference the financial accounting and reporting guidance for real estate time-sharing transactions that is provided in AICPA Statement of Position (SOP) 04-2, *Accounting for Real Estate Time-Sharing Transactions*. This Statement also amends FASB Statement No. 67, *Accounting for Costs and Initial Rental Operations of Real Estate Projects*, to state that the guidance for (1) incidental operations and (2) costs incurred to sell real estate projects does not apply to real estate time-sharing transactions. The accounting for those operations and costs is subject to the guidance in SOP 04-2. This statement is effective for financial statements for fiscal years beginning after June 15, 2005, with earlier application encouraged. Recom has evaluated the impact of the adoption of SFAS 152, and does not believe the impact will be significant to the company's overall results of operations or financial position since Recom does not enter into such transactions.

In December 2004, the FASB issued SFAS No.153, *Exchanges of Nonmonetary Assets, an amendment of APB Opinion No. 29, Accounting for Nonmonetary Transactions*. The amendments made by Statement 153 are based on the principle that exchanges of nonmonetary assets should be measured based on the fair value of the assets exchanged. Further, the amendments eliminate the narrow exception for nonmonetary exchanges of similar productive assets and replace it with a broader exception for exchanges of nonmonetary assets that do not have commercial substance. Previously, Opinion 29 required that the accounting for an exchange of a productive asset for a similar productive asset or an equivalent interest in the same or similar productive asset should be based on the recorded amount of the asset relinquished. Opinion 29 provided an exception to its basic measurement principle (fair value) for exchanges of similar productive assets. The FASB believes that exception required that some nonmonetary exchanges, although commercially substantive, be recorded on a carryover basis. By focusing the exception on exchanges that lack commercial substance, the FASB believes this statement produces financial reporting that more faithfully represents the economics of the transactions. SFAS 153 is effective for nonmonetary asset exchanges occurring in fiscal periods beginning after June 15, 2005. Earlier application is permitted for nonmonetary asset exchanges occurring in fiscal periods beginning after the date of issuance. The provisions of SFAS 153 shall be applied prospectively. Recom has evaluated the impact of the adoption of SFAS 153, and does not believe the impact will be significant to the company's overall results of operations or financial position.

In December 2004, the FASB issued SFAS No.123 (revised 2004), *Share-Based Payment*. SFAS 123(R) will provide investors and other users of financial statements with more complete and neutral financial information by requiring that the compensation cost relating to share-based payment transactions be recognized in financial statements. That cost will be measured based on the fair value of the equity or liability instruments issued. SFAS 123(R) covers a wide range of share-based compensation arrangements including share options, restricted share plans, performance-based awards, share appreciation rights, and employee share purchase plans. SFAS 123(R) replaces FASB Statement No. 123, *Accounting for Stock-Based Compensation*, and supersedes APB Opinion No. 25, *Accounting for Stock Issued to Employees*. SFAS 123, as originally issued in 1995, established as preferable a fair-value-based method of accounting for share-based payment transactions with employees. However, that statement permitted entities the option of continuing to apply the guidance in Opinion 25, as long as the footnotes to financial statements disclosed what net income would have been had the preferable fair-value-based method been used. Public entities (other than those filing as small business issuers) will be required to apply SFAS 123(R) as of the first interim or annual reporting period that begins after June 15, 2005. SFAS 123(R) is applicable for Recom

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effective the first interim period that starts after December 15, 2005. Recom has evaluated the impact of the adoption of SFAS 123(R), and believes that the impact will be significant to the company's overall results of operations and financial position (a pro forma effect, as estimated by management, is disclosed earlier in this note).

In December 2004 the Financial Accounting Standards Board issued two FASB Staff Positions FSP FAS 109-1, *Application of FASB Statement 109 "Accounting for Income Taxes" to the Tax Deduction on Qualified Production Activities Provided by the American Jobs Creation Act of 2004,* and FSP FAS 109-2 *Accounting and Disclosure Guidance for the Foreign Earnings Repatriation Provision within the American Jobs Creation Act of 2004.* Neither of these affected the Company as it does not participate in the related activities

In January 2003, the FASB issued FASB Interpretation No. ("FIN") 46, "Consolidation of Variable Interest Entities" ("FIN 46"). In December 2003, FIN 46 was replaced by FASB interpretation No. 46(R) "Consolidation of Variable Interest Entities." FIN 46(R) clarifies the application of Accounting Research Bulletin No. 51, "Consolidated Financial Statements," to certain entities in which equity investors do not have the characteristics of a controlling financial interest or do not have sufficient equity at risk for the entity to finance its activities without additional subordinated financial support from other parties. FIN 46(R) requires an enterprise to consolidate a variable interest entity if that enterprise will absorb a majority of the entity's expected losses, is entitled to receive a majority of the entity's expected residual returns, or both. FIN 46(R) is effective for entities being evaluated under FIN 46(R) for consolidation no later than the end of the first reporting period that ends after March 15, 2004. The Company does not currently have any variable interest entities that will be impacted by adoption of FIN 46(R).

**3.**

**PROPERTY AND EQUIPMENT**

Our property and equipment as of December 31, 2004 is as follows:

| | |
|---|---|
| Computer equipment | $ 87,064 |
| Leasehold improvements | 66,792 |

| | |
|---|---|
| Furniture and fixtures | 50,000 |
| Software | 15,904 |
| Other equipment | 22,434 |
| Total property and equipment | 242,194 |
| Accumulated depreciation | 98,588 |
| Property and equipment, net | $ 143,606 |

Depreciation expense amounted to $58,837 and $39,058 during the years ended December 31, 2004 and 2003, respectively.

**4.**

**PATENTS AND TECHNOLOGY**

On September 19, 2002, we acquired certain know how, trade secrets and other proprietary intellectual property rights relating to the development of a human biomedical signal amplification equipment and technology from ARC Finance Group, LLC ( *ARC Finance* ) in exchange for 23,400,000 shares of common stock (7,800,000 shares pre-split). As a result of this transaction, ARC Finance acquired approximately

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84.5% of the company s outstanding shares. We have valued the technology and the common stock issued at $78,023, which was ARC Finance Group s historical cost basis for the patents.

When we acquired the patent, we inherited a licensing agreement and therefore consider the patent to have been placed in service. We are amortizing our initial patent, valued at $78,023, over an estimated useful life of 7 years. The aggregate amortization expense will be approximately $56,000 over the next five years, with an expense of approximately $11,200 annually. The remaining balance in the intangible account consists of additional costs relating to our amplification technology, principally patent application costs. We have one patent and five patent applications concerning our proprietary amplification technology. We have recorded the value of our original patent and the rights to our amplification technology at their historical cost of $352,974, with accumulated amortization of $22,292 as of December 31, 2004. Amortization expense amounted to $11,146 and $11,146 during the years ended December 31, 2004 and 2003, respectively.

**5.**

**CONTINGENT SETTLEMENT PAYABLE**

In conjunction with Dr. Budimir Drakulic becoming our Vice President and Chief Technology Officer, we reached an agreement-in-principle with Dr. Drakulic to offer to sell common shares to certain individuals in order to protect our rights to the Signal Technologies. As part of that agreement, we agreed that should we raise more than $2 million in certain offerings, we would pay 4% of the proceeds of those offerings greater than $2 million to those individuals up to a maximum amount of $480,350. At December 31, 2003, our potential obligation related to this agreement was $104,201. We subsequently reached settlements with a number of these individuals and the remaining liability related to the agreement as of December 31, 2004 is $21,113, which is included in accounts payable and accrued expenses. See Note 11, *Commitments And Contingencies* .

**6.**

**INCOME TAXES**

We have eliminated substantially all prior net operating loss carryovers due to change of ownership in September 2002. We have provided no current income taxes due to the losses incurred in 2002 through 2004. Net operating losses for tax purposes of $9,325,876 at December 31, 2004 are available for carryover. The net operating losses will expire from 2022 through 2024. We have provided a 100% valuation allowance for the deferred tax benefit resulting from the net operating loss carryover due to our limited operating history since the change of control. In addressing the realizability of deferred tax assets, management considers whether it is more likely than not that some portion or all of the deferred tax assets will not be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income during the periods in which those temporary differences are deductible. A reconciliation of the statutory Federal income tax rate and the effective income tax rate for the years ended December

31, 2004 and 2003 follows:

| | **December 31, 2004** | **December 31, 2003** |
|---|---|---|
| Statutory federal income tax rate | (35)% | (35)% |
| State income taxes, net of federal taxes | (8)% | (8)% |
| Non-deductible items | 8% | 13% |
| Valuation allowance | 35% | |

30%

Effective income tax rate

0%

0%

Significant components of deferred tax assets and liabilities are as follows:

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| | December 31, 2004 | December 31, 2003 |
|---|---|---|
| Deferred tax assets (liabilities): | | |
| Net operating loss carryforwards | $ 3,264,057 | $ 1,391,535 |
| Deferred compensation | 3,803,881 | |

| | | |
|---|---|---|
| | | 3,267,687 |
| Depreciation and amortization | | |
| | | (22,018) |
| | | (18,276) |
| Deferred tax assets, net | | |
| | | 7,045,920 |
| | | 4,640,946 |
| Valuation allowance | | |
| | | (7,045,920) |
| | | (4,640,946) |
| Net deferred tax assets | | |
| | $ | |
| | $ | |

**7.**

**UNIT OFFERING**

During October 2003, we sold 53.2875 units in a private placement, with each unit consisting of 33,334 series A preferred shares and 16,667 class C common share purchase warrants, at a price of $100,000 per unit. The proceeds to our company, net of expenses, were approximately $4,806,000. Each class C warrant entitles the holder to purchase one common share at an exercise price of $3.75 per share. The class C warrants are exercisable anytime during the four year period commencing on the final closing and do not contain provisions for cashless exercise. On October 1, 2004, we voluntarily reduced the exercise price of the class C warrants from $3.75 to $3. The aggregate number of warrants which have been repriced is 896,488. The excess of the value of the modified warrants as compared to the original warrants was calculated according to SFAS 123. As a result of this repricing, Recom has recorded a non-cash expense of $158,516 for the excess value during the fourth quarter of 2004.

We issued to the placement agent who facilitated the private placement of the Units a warrant exercisable into 179,292 units, each unit comprising one series A preferred share and a common share purchase warrant exercisable into one-half common share at $3.75 per share and valued at $238,430 using the Black Scholes model. The placement agent s warrant is exercisable at $3.60 per share and expires five years following the date of issuance.

In accordance with EITF 00-27, a portion of the proceeds were allocated to the class C warrants based on their relative fair value, which totaled $949,121 using the Black Scholes option pricing model. Further, we attributed a beneficial conversion feature of $896,474 to the series A preferred shares based upon the difference between the conversion price of those shares and the closing price of our common shares on the date of issuance. The assumptions used in the Black Scholes model are as follows: (1) dividend yield of 0%; (2) expected volatility of 81.16%, (3) weighted average risk-free interest rate of 1.68%, and (4) expected life of 1.5 years as the conversion feature and warrants are immediately exercisable. Both the fair value of the class C warrants and the beneficial conversion feature were recorded as a dividend and are included in the accompanying financial statements.

Our series A preferred shares carry a liquidation value equal to $3 per share, are senior to all other shares of capital stock now existing or hereinafter created by our company as to dividend and liquidation rights, and have voting rights as if converted into common shares. Each series A preferred shareholder has the option at any time to convert all or any portion of his or her shares into common shares on a one-for-one basis. During 2004, 1,546,633 series A preferred shares were converted into an equivalent number of common shares.

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Our series A preferred shares are required to pay dividends of 8% annually ($107,575 accrued and included in accounts payable and accrued expenses as of December 31, 2003), to be paid quarterly either in cash or in the form of additional preferred shares at the discretion of Recom. Any series A preferred shares issued as a dividend will be valued at $3 per share. During 2004 and 2003, we accrued dividends in the amount of $295,452 and $107,575, respectively, with respect to our series A preferred shares, for a total of $403,027 since original issuance in 2003. We have elected to pay these dividends in kind through the issuance of additional preferred stock. During 2004, in satisfaction of the accrued dividends, we issued or committed to issue a total of 134,834 preferred shares valued at $404,487. As of December 31, 2004, 3,457 shares were converted into common shares. As of December 31, 2004 there are no accrued dividends payable reflected on the balance sheet.

We can force conversion of the series A preferred shares into common shares upon 45 days written notice to the holders of the series A convertible preferred stock, if (1) our common shares are listed on a qualified exchange (NASDAQ, AMEX or NYSE); (2) the closing price of our common shares is at least $7.50 for 30 consecutive trading days; and (3) the common shares underlying the conversion are subject to an effective registration statement filed with the SEC pursuant to the Securities Act of 1933.

**8.**

**CONVERTIBLE DEBENTURE PAYABLE**

On December 29, 2004, we sold an 8% convertible debenture in the amount of $2,000,000 (effective interest rate of 89%) to DKR SoundShore Oasis Holding Fund Ltd. Terms call for the payment of $400,000 in principal on the debenture in cash on May 16, 2005, June 1, 2005, July 1, 2005, August 1, 2005 and August 31, 2005, respectively. The debenture also calls for payments of interest on the outstanding principal on the debenture in cash on May 10, 2005, June 1, 2005, July 1, 2005, August 1, 2005 and August 31, 2005, respectively.

For so long as the debenture is unpaid, the debenture holder is entitled to convert the debenture into a number of common shares equal to the outstanding principal on the debenture divided by $5.25, such amount representing 105% of the closing price for our common shares on the trading day prior to the sale of the debenture. We also have the right to pay the principal and interest on the debenture in common shares in lieu of cash provided that we first register those shares with the SEC, are not otherwise in default under the debenture, and have satisfied certain other conditions including notice requirements. Should payment be made in common shares, the principal and interest under the debenture subject to conversion would be convertible into those shares at the rate of 85% of the average of the three lowest closing prices for those shares during the ten day period prior to the repayment date. If we elect to pay only interest with common shares, the conversion rate shall be fixed at 90% of the closing price immediately prior to the payment or delivery date.

While pre-payment of the debenture is generally not allowed before its August 31, 2005 due date without the consent of the debenture holder, we may do so in cash so long as we pay the entire outstanding balance due through maturity and also pays a 10% premium on the outstanding principal.

In the event of default under the debenture, including both failure to make principal and interest payments and failure to comply with various covenants, the interest rate will increase to 15%, and we will be obligated to pay the greater of (1) the principal due under the debenture together with a 30% premium, plus interest accrued; or (2) the principal due under the debenture, plus interest accrued, divided by conversion price were the debenture holder to elect to convert the debentures into common shares.

As additional consideration for the purchase of the debenture, we granted to the debenture holder warrants entitling it to purchase 275,000 common shares at the price of $5.75 per share, or 115% of the closing price for those shares on the trading day prior to the sale of the debenture. These warrants lapse if unexercised by December 29, 2009. A registration rights agreement was executed requiring Recom to register the shares of

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its common stock underlying the debenture and warrant so as to permit the public resale thereof. The debenture provided for the payment of liquidated damages of 2% of the debenture balance per month if the stipulated registration deadlines were not met. In accordance with EITF 00-27, a portion of the proceeds were allocated to the warrant liability based on its fair value, which totaled $447,570 using the Black Scholes option pricing model. The remaining balance was allocated to the convertible debt instrument and was used to compute the beneficial conversion feature. We attributed a beneficial conversion feature of $408,333 to the convertible debenture based upon the difference between the effective conversion price of those shares and the closing price of our common shares on the date of issuance. The assumptions used in the Black Scholes model are as follows: (1) dividend yield of 0%; (2) expected volatility of 91%, (3) risk-free interest rate of 3.12%, and (4) expected life of 1.5 years. Additionally, we incurred legal costs of $31,660 in connection with the sale of the debenture. The total debt discount of $887,563 is being amortized over the term of the debenture. During the year ended December 31, 2004, amortization as interest expense amounted to $13,842.

In conjunction with raising capital through the issuance of convertible debt, the Company has issued a warrant that has registration rights for the underlying shares. As the contract must be settled by the delivery of registered shares and the delivery of the registered shares is not controlled by the Company, pursuant to EITF 00-19, Accounting for Derivative Financial Instruments Indexed to, and Potentially Settled in, a Company s Own Stock , the net value of the warrants at the date of issuance was recorded as a warrant liability on the balance sheet ($447,570) and the change in fair value from the date of issuance to December 31, 2004 has been included in other income (expense). Upon the registration statement being declared effective, the fair value of the warrant on that date will be reclassified to equity (see Note 13).

For the year ended December 31, 2004 the change in fair value of the warrant issued with registration rights increased by approximately $130,430 to $578,000 at December 31, 2004 and is recognized in other expense.

**9.**

**OTHER STOCKHOLDERS EQUITY TRANSACTIONS**

**Non-Related Party Equity Transactions**

On April 28, 2004, we granted to a shareholder warrants to purchase 250,000 common shares at $7.90 per share pursuant to a legal settlement. As part of this settlement, we agreed to register 80,000 common shares previously held by the shareholder, and the shareholder agreed that an additional 369,000 common shares previously held by the shareholder would be cancelled upon the registration of the 80,000 shares. The warrants are exercisable on August 1, 2004, and lapse if unexercised on July 31, 2007. The fair value of the warrants was estimated at $757,207 under the Black-Scholes option-pricing model computed as of the date of grant using the following assumptions: (1) dividend yield of 0%, (2) expected volatility of 81.17%, (3) weighted-average risk-free interest rate of 2.45%, and (4) expected life of 1.5 years. In July 2004, the shareholder agreed to cancel the warrants in consideration of a payment to the warrant holder in the amount of $14,500, all of which has been charged to general and administrative expense.

During 2004, we issued 130,030 common shares pursuant to exercises of class A warrants issued as part of a financing transaction in May 2003. We received cash payments of $275,000 related to these exercises.

During 2004, we issued 16,665 common shares pursuant to exercises of class C warrants issued as part of the unit offering in October 2003. We received cash payments of $49,996 related to these exercises.

During 2004, we issued 51,815 common shares related to cashless exercises of class A warrants originally issued as part of a financing transaction in May 2003. As a result of the cashless exercise provision, 14,852 options were cancelled. We received no cash payments related to these exercises.

During 2004, we issued in the aggregate 453,143 common shares for marketing, legal and business services**.** We valued these services at $1,900,774 based upon the fair market value of our common shares determined

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as the closing stock price as reported by the OTCBB at the date of issuance. Of those shares issued, 52,391 common shares valued at $190,140 were expensed during the fourth quarter of 2003 since the services were rendered during that period.

During 2004, we issued in the aggregate 254,000 common share purchase options to employees and members of our board of directors. All options were issued at an exercise price equal to the closing market price as reported by the OTCBB on the date of issuance. Of those grants: (1) 50,000 options were issued in January 2004, vested immediately and are exercisable at a price of $3.50 per share; (2) 80,000 options were issued in January 2004, vest quarterly over a four year time period and are exercisable at $3.60 per share; (3) 28,000 options were issued in February 2004, vest quarterly over a one year time period and are exercisable at $3.70 per share; (4) 10,000 options were issued in April 2004, vest quarterly over a one year time period and are exercisable at $6.00 per share; (5) 28,000 options were issued in June 2004, vest quarterly over a one year time period and are exercisable at $6.25 per share; (6) 2,000 options were issued in July 2004, vest quarterly over a one year time period and are exercisable at $3.95 per share; (7) 28,000 options were issued in October 2004, vest quarterly over a one year time period and are exercisable at $2.29 per share; and (8) 28,000 options were issued in November 2004, vest quarterly over a one year time period and are exercisable at $2.90 per share.

In March 2003, we issued 21,000 warrants at an exercise price of $0.81 per share, for which we recognized a total of $13,927 in expense for services rendered. The fair value of warrants was recorded using the Black Scholes option-pricing model computed as of the date of grant using the following assumptions: (1) dividend yield of 0%, (2) expected volatility of 158.48%, (3) weighted-average risk-free interest rate of 3.13%, and (4) expected life of 1.5 years.

In March 2003, our Board of Directors approved the issuance of five-year warrants to purchase 900,000 shares (300,000 pre-split) of our common shares at $0.50 per share to a firm which we retained to perform various services including: introductions to investment banking firms; assistance in the structuring of private offerings; assistance in capital market transactions, mergers and acquisitions; advisory services; and assistance in developing strategic relationships. We estimated the fair value of the warrants at $657,779 under the Black-Scholes option-pricing model computed as of the date of grant using the following assumptions: (1) dividend yield of 0%, (2) expected volatility of 158.48%, (3) weighted-average risk-free interest rate of 1.65%, and (4) expected life of 1.5 years.

On April 15, 2003, we granted to Brookstreet Securities Corporation warrants to purchase 200,000 common shares pursuant to an investment banking agreement. The warrants were issued in four tranches of 50,000 each, with the first tranche of 50,000 fully vested and exercisable at $1.25 per share. The second tranche vested 90 days after the date of the agreement with an exercise price of $2.25 per share; the third tranche 180 days with an exercise price of $3.25 per share; and the fourth tranche in 270 days with an exercise price of $4.25 per share. We estimated the fair value at $418,187 under the Black Scholes option-pricing model computed as of the measurement date, which is the date the services were performed, using the following assumptions: (1) dividend yield of 0%, (2) expected volatility range of 53.84% to 114.24%, (3) weighted-average risk-free interest rate range of 1.42% to 2.57%, and (4) expected life of 1.5

years.

In May 2003, we completed the first tranche of a private placement pursuant to which we sold 82,667 units to three investors at $3.00 per unit for cash amounting to $248,000. Each unit consisted of one common share and one common share purchase warrant. Each warrant was exercisable at $3.00 until May 14, 2004. Upon exercise of the warrants each investor was entitled to receive one common share and an additional common share purchase warrant entitling him or her to purchase one additional common share at $6.00 per share until November 15, 2004.

On June 20, 2003, our board of directors amended our articles of incorporation to increase our authorized capitalization to 110,000,000 shares, designating 100,000,000 to common stock and 10,000,000 to preferred

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stock. Our board of directors is authorized under our articles of incorporation to provide from time to time for the issuance of preferred shares in series and to fix and determine from time to time, before issuance, the designation and relative rights and preferences of the shares of each series of preferred stock and the restrictions or qualifications. See Note 6, *Unit Offering* .

On June 2, 2003, pursuant to a consulting agreement, we granted to a consultant common share purchase warrants entitling him to purchase 108,000 common shares at $2.40. We estimated the fair value of the warrants at $199,226 under the Black-Scholes option-pricing model computed as of the date of grant using the following assumptions: (1i) dividend yield of 0%, (2) expected volatility of 114.24%, (3) weighted-average risk-free interest rate of 1.42%, and (4) expected life of 1.5 years.

On July 17, 2003 we retained Maxim Group, LLC ( *Maxim* ), a New York based investment banking firm, to act as our lead investment bank. Under that agreement Maxim provides us with, among other services, assistance with our financing efforts in securing additional capital for product development and to fund the process of gaining approval for our cardiac monitoring device by the FDA. Maxim also agreed to assist us with general business strategy and with seeking a listing on a national exchange. We paid Maxim $50,000 at the inception of the agreement, with additional $7,500 per month payments through June 30, 2004. In addition, we issued Maxim share purchase warrants entitling it to purchase 100,000 restricted common shares at $4.92 per share. We estimated the fair value of the warrants at $133,349 under the Black-Scholes option-pricing model computed as of the date of grant using the following assumptions: (1) dividend yield of 0%, (2) expected volatility of 81.16%, (3) weighted-average risk-free interest rate of 1.68%, and (5) expected life of 1.5 years.

In July 2003, we closed the second tranche of a private placement by selling 75,075 units to four investors at $3.33 per unit for total cash of $250,000. Each unit consisted of one common share and one common share purchase warrant. Each warrant was exercisable at $3.33 until May 14, 2004. Upon exercise of the warrants each investor was entitled to receive one common share and an additional common share purchase warrant entitling him or her to purchase one additional common share at $6.66 per share until November 15, 2004.

In August 2003, we entered into voluntary trading restriction agreements with three shareholders in exchange for share purchase warrants entitling them to purchase a total of 23,501 common shares at a price of $3.29 per share. In September 2003, we entered into a voluntary trading restriction agreement with a shareholder in exchange for share purchase warrants entitling him to purchase 18,000 common shares at 85% of the closing price of the shares on the date of the agreement ($5.29 at September 23, 2003). We estimated the fair value of the warrants at $74,088 under the Black Scholes option-pricing model computed as of the date of grant using the following assumptions: (1) dividend yield of 0%, (2) expected volatility of 81.16%, (3) weighted-average risk-free interest rate of 1.68%, and (4) expected life of 1.5 years.

In September 2003, we issued to a consultant share purchase warrants entitling him to purchase 25,000 common shares at an exercise price of $3.29 per share. We estimated the fair value of the warrants at $41,202 under the Black

Scholes option-pricing model computed as of the measurement date, which is the date that the services were performed, using the following assumptions: (1i) dividend yield of 0%, (2) expected volatility of 81.16%, (3) weighted-average risk-free interest rate of 1.68%, and (4) expected life of 1.5 years

In September 2003, we issued 305,000 restricted common shares to three persons pursuant to the cashless exercise provisions of common shares purchase warrants held by such persons.

In November 2003, we issued 800,000 restricted common shares to an investment banking company pursuant to the cashless exercise provisions of common share purchase warrants held by such company.

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During 2003, we issued in the aggregate 367,514 common shares for marketing and business services rendered during the period. We valued these services at $1,233,502 based upon the fair market value of the shares determined as the closing stock price as reported on the OTCBB system, at the date of issuance.

We issued 150,000 shares (50,000 shares pre-split) of its common stock during the year ended December 31, 2001 to various consultants and service providers as partial compensation for services rendered to the company. These shares were valued at $5,000.

**Related Party Equity Transactions**

During the years ended December 31, 2002, 2001 and 2000, our President and majority shareholder at that time contributed $56,400, $45,000 and $35,000 for working capital purposes.

On September 19, 2002, our President at that time purchased for the sum of $125,000 a common share purchase warrant entitling him to purchase 600,000 (200,000 pre-split) common shares at an exercise price of $0.667 per share, which was above the current market price at the date of issuance. The warrant could not be exercised before September 1, 2003, expires in September 2006, and contains cashless exercise options and certain anti-dilution and other provisions.

On September 19, 2002, we acquired certain know how, trade secrets and other proprietary intellectual property rights relating to the development of a human biomedical signal amplification equipment and technology, referred to in these financial statement as the "Signal Technologies", from ARC Finance Group, LLC ( ARC ) in exchange for 23,400,000 shares of common stock (7,800,000 shares pre-split). As a result of this transaction, ARC acquired approximately 84.5% of our outstanding shares. We have valued the issuance of the common stock at $78,023, which was ARC Finance Group s historical cost basis for the patents.

On October 12, 2002, we agreed to issue a total of 2,100,000 (700,000 pre-split) shares of our common stock to Marvin H. Fink pursuant to a four-year employment agreement under which Mr. Fink would serve our Chief Executive Officer and Chairman of our board of directors. We valued the aforesaid grant of 2,100,000 common shares at $15,190, reflecting the current market value for our common shares on the measurement date. These shares vest at the rate of 8.33% or 174,999 (58,333 pre-split) shares per quarter with the first vesting on January 12, 2003. We are expensing the value of the shares over the life of the employment agreement, and have expensed $5,063 during each of the years ended December 31, 2004 and 2003, with the remainder presented as deferred compensation in Stockholders Equity. We have also estimated that the services performed by Mr. Fink for $1 per year have a annual value of $80,000. In order to fairly present the value of these services, we have recorded additional annual expenses of $80,000, $80,000 and $20,000 for the years ended December 31, 2004, 2003 and 2002, respectively, which was classified as contributed capital. For a description of the employment agreement, see Note 11, *Commitments And Contingencies* .

On October 15, 2002, we agreed to issue a total of 600,000 (200,000 pre-split) common shares to B World Technologies, Inc., pursuant to a Loanout Agreement with Dr. Budimir Drakulic and B World Technologies. Under that agreement, Dr. Drakulic is obligated to work as an independent contractor for Recom and serve as our Vice President and Chief Technology Officer for a term of ten years. We valued the aforesaid grant of 600,000 common shares at $4,140, the current market value for our common shares on the measurement date. These shares vest at the rate of 5% or 30,000 (10,000 pre-split) shares per quarter with the first shares vesting on January 15, 2003. We have expensed the value over the life of the agreement and have expensed $828 during each of the years ended December 31, 2004 and 2003, with the remainder presented as deferred compensation in Stockholders Equity. For a description of the Loanout Agreement, see Note 0, *Commitments And Contingencies* .

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Effective October 15, 2002, we agreed to issue a total of 225,000 (75,000 pre-split) common shares to Mr. Ellsworth Roston, who later became a director of the company, pursuant to a two-year consulting agreement whereby Mr. Roston would consult with Recom with respect to the engineering, development and refining of our technologies. We valued the shares at $1,553, the current market value for our common shares on the measurement date. These shares vest at the rate of 12.5% or 28,125 (9,375 pre-split) shares per quarter with the first shares vesting on February 1, 2003. We are expensing the value over the life of the agreement of which $629 and $777 was expensed during the years ended December 31, 2004 and 2003, respectively, with the remainder presented as deferred compensation in Stockholders Equity. For a description of the consulting agreement, see Note 11, *Commitments And Contingencies*.

On October 30, 2002, Mr. Roston became a director of the company and for $190,000 purchased 71,250 (23,750 pre-split) common shares and a five-year warrant to purchase 450,000 (150,000 pre-split) common shares at an exercise price of $1.667 per share.

On October 22, 2002, we issued a total of 564,810 (188,270 pre-split) common shares to eleven individuals for total cash consideration of $17,786, pursuant to an agreement which was entered into in conjunction with Dr. Budimir Drakulic becoming our Vice President and Chief Technology Officer and also in order to protect our rights to the acquired patented signal technologies. On October 11, 2002, we issued a five-year warrant to purchase 375,000 (125,000 pre-split) common shares for $0.007 per share exercisable immediately to one of the individuals mentioned above who also received common shares. We estimated the fair value of warrants at $5,324, which was expensed as of December 30, 2002, using the Black Scholes option-pricing model computed as of the date of grant using the following assumptions: (1) dividend yield of 0%, (2) expected volatility of 120.25%, (3) weighted-average risk-free interest rate of 3.01%, and (4) expected life of 1.25 years.

In February 2003, we issued 216,000 options, in two tranches, to Mr. Lowell Harmison, who later became a director of our company, for consulting work related to helping us with the FDA review process for our heart monitoring device. The first tranche of options, which are fully vested, allow Mr. Harmison to purchase 108,000 common shares (36,000 shares pre-split) at $0.97 per share, exercisable over five years. The second tranche of 108,000 options vest over three years on a quarterly basis. We estimated the fair value of the first tranche of 108,000 options at $80,456 using the Black Scholes option-pricing model computed as of the grant date with the following assumptions: (1) dividend yield of 0%, (2) expected volatility of 158.48%, (3) weighted-average risk-free interest rate of 1.65%, and (4) expected life of 1.5 years. The value of the second tranche of 108,000 options is measured on the vesting dates to reflect the dates that the services are completed. During 2003, there were three quarterly vestings which were fair valued with the Black Scholes model at $74,643. The following assumptions were used in the model: (1) dividend yield of 0%, (2) expected volatility range between 53.84% and 114.24%, (3) weighted average risk free rate of between 1.42% and 1.86%, and (4) expected life of 1.5 years. During 2004 there were four quarterly vestings which were fair valued with the Black Scholes model at $118,752 and have been expensed as they vest. The following assumptions were used in the model for 2004: (1) dividend yield of 0%, (2) expected volatility range between 81.17% and 90.75%, (3) weighted average risk free rate of between 1.69% and 2.56%, and (4) expected life of 1.5 years. For a description of the consulting agreement, see Note 11, *Commitments And Contingencies*.

In March 2003, we entered into a consulting agreement with our then CFO for certain financial and accounting services, and issued him options to purchase 900,000 (300,000 pre-split) common shares at $0.95 per share. These options, which were issued as compensation for services, vest quarterly over a 3-year period. The agreement was terminated in November 2003 with 150,000 options having vested over two quarters. We estimated the fair value of the options at $574,196 under the Black-Scholes option-pricing model computed as of the date the services were rendered using the following assumptions: (1) dividend yield of 0%, (2) expected volatility range of 81.16% to 114.24%, (3) weighted-average risk-free interest rate of 1.42% to 1.68%, and (4) expected life of 1.5 years.



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On April 1, 2003, we completed a private placement of 112,792 (37,604 pre-split) common shares or total consideration of $250,000 to the spouse of the owner of ARC Finance Group, LLC, our principal shareholder. The consideration included $100,000 in cash and the cancellation of $150,000 of debt previously advanced for $33,208 in expenses and $116,792 of furniture and fixtures and leasehold improvements from a related party.

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**OPTIONS AND WARRANTS OUTSTANDING**

**Stock Plans**

On November 1, 2002, our Board of Directors approved the establishment of the 2002 Stock Plan (the *2002 Stock Plan* ). Our shareholders approved the plan on June 5, 2003. The total number of common shares available for grant and issuance under the plan may not exceed 6,000,000 (2,000,000 pre-split) shares, subject to adjustment in the event of certain recapitalizations, reorganizations and similar transactions. Common stock purchase options may be exercisable by the payment of cash or by other means as authorized by the committee or the Board of Directors. At December 31, 2004, we had issued 2,141,000 common share purchase options under the plan.

On March 31, 2003, our Board of Directors approved the establishment of the 2003 Nonqualified Stock Option And Stock Plan (the *2003 Stock Plan* ). The 2003 Stock Plan allows the Board to grant common stock purchase options or issue free-trading or restricted common stock from time to time to our employees, officers, directors and consultants. The total number of common shares available for grant and issuance under the plan may not exceed 1,500,000 (500,000 pre-split) shares, subject to adjustment in the event of certain recapitalizations, reorganizations and similar transactions. Options may be exercisable by the payment of cash or by other means as authorized by the Board of Directors. Options granted under the 2003 Stock Plan will not qualify under Section 422 of the Internal Revenue Code as incentive stock options. At December 31, 2004, we had issued 792,157 common shares under the plan, and no options.

**Common Share Options And Warrants Issued**

The following table summarizes information on all common share purchase options and warrants issued by the company for the periods ended December 31, 2004 and 2003, including and common share equivalents relating series A preferred share purchase warrants.

**December 31, 2004**

| | December 31, 2003 | | | |
|---|---|---|---|---|
| | **Number** | **Weighted Average Exercise Price** | **Number** | **Weighted Average Exercise Price** |
| Outstanding at beginning of the period | 5,920,669 | $ 1.77 | 1,425,000 | $ 0.80 |
| Granted during the period | 809,030 | 5.82 | 5,700,669 | |

| | |
|---|---|
| | 1.75 |
| Exercised during the period | |
| | 228,362 |
| | 2.34 |
| | 1,105,000 |
| | 0.54 |
| Terminated during the period | |
| | 1,842,443 |
| | 1.85 |
| | 100,000 |
| | 0.50 |
| Outstanding at end of the period | |
| | 4,658,894 |
| | 2.27 |
| | 5,920,669 |
| | 1.77 |
| Exercisable at end of the period | |

3,864,270

$ 2.43

2,756,368

$ 1.18

The number and weighted average exercise prices of all common shares and common share equivalents issuable under and stock purchase options and warrants outstanding as of December 31, 2004 and 2003 is as follows:

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| Range of Exercise Prices | Remaining Number Outstanding | Weighted Average Contractual Life (Years) | Weighted Average Exercise Price |
|---|---|---|---|
| $0 to 1 | 2,033,632 | 3.0 | $ 0.90 |

| | | | |
|---|---|---|---|
| 1 to 2 | 450,000 | 2.8 | $ 1.67 |
| 2 to 3 | 174,000 | 3.9 | $ 2.49 |
| 3 to 4 | 1,417,262 | 3.7 | $ 3.16 |
| 4 to 5 | 256,000 | 3.7 | |

$ 4.53

5 to 6

293,000

4.7

$ 5.72

6 to 7

35,000

4.3

$ 6.20

**11.**

**COMMITMENTS AND CONTINGENCIES**

Recom has employed Mr. Marvin H. Fink as our Chief Executive Officer and President under a four-year employment agreement entered into effective as of October 12, 2002. The essential terms of the employment agreement are as follows: (1) Mr. Fink is paid $1 per year in base salary; (3) Mr. Fink was granted 2,100,000 restricted common shares (700,000 shares pre-split), to be earned over three years of continuous employment; (3) Mr. Fink is entitled to a grant of 250,000 common shares upon Recom achieving $0.50 in fully-diluted earnings per share; (4) Mr. Fink is entitled to a grant of 600,000 common shares (200,000 shares pre-split) should our common shares be listed on any of the NYSE, AMEX or Nasdaq national stock exchanges or markets; (5) , Mr. Fink is entitled to a grant of 600,000 common shares (200,000 shares pre-split) in the event of a change in control; and (6) Mr. Fink is entitled to a number of employee benefits under the agreement, including a $1,200 per month automobile allowance, individual medical plan reimbursement of up to $2,000 per month until we adopt a group plan for our employee s, and the right to participate in all benefit plans established for our employees or executives, including medical, hospitalization, dental, long-term care and life insurance programs. The employment agreement provides for early termination in the case of Mr. Fink s death or disability, Mr. Fink s termination by Recom for cause as that term is defined in the agreement;

Mr. Fink s termination of employment for good reason as that term is defined in the agreement, a change in ownership as that term is defined in the agreement, or sixty days prior notice by Mr. Fink.

Recom has engaged Dr. Budimir Drakulic as our Vice President and Chief Technology Officer on a part-time independent contractor basis under a loan-out agreement dated October 15, 2002 with two companies, B World Technologies, Inc. and B Technologies, Inc., and Dr. Drakulic individually. Dr. Drakulic is the president and owner of these companies. The essential terms of the agreement are as follows: (1) the agreement provides for a ten-year initial term, with annual renewal provisions thereafter; (2) B Technologies was entitled to a $10,000 bonus upon execution, and to monthly service fee of $15,000 thereafter; (3) we granted 600,000 (200,000 shares pre-split) restricted common shares to B World Technologies, to be earned over five years of continuous provision of services by Dr. Drakulic. The loan-out agreement provides for early termination should B World and B Technologies fail, neglect or refuse to provide Dr. Drakulic s services. In such an event, all compensation under the agreement will terminate and the unvested portion of the 600,000 restricted common share grants shall be deemed forfeit as of the effective termination date.

Since March 1, 2003, Dr. Drakulic has worked for us on a full-time basis even though the loan-out agreement only provides for the provision of part-time services. We have agreed to characterize these additional services as being provided by Dr. Drakulic as an employee, and to pay him $7,500 annually as compensation for their provision. Since January 1, 2004, this annual compensation was increased to $37,000. On March 10, 2003, as additional incentive for the performance of Dr. Drakulic, we granted to B World

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Technologies options entitling it to purchase 750,000 common shares at $0.95 per share. These options vest quarterly over a four year term, and lapse, if not exercised, on March 9, 2008.

Mr. Ellsworth Roston, one of our directors, provides consulting services to Recom under a two-year agreement dated November 1, 2002. Under this agreement, Mr. Roston provides advice relating to engineering, developing and refining our products and technologies. Mr. Roston also agreed under the agreement to act as a member of our board of directors during its term. Mr. Roston is a patent attorney who handles our patent work. The agreement specifically provides that the consulting services provided by Mr. Roston will not include any legal work, for which we will compensate him separately. In compensation for his consulting services, we granted 225,000 (75,000 shares pre-split) restricted common shares to Mr. Roston. See Note 9, *Other Equity Transactions* .

Dr. Lowell T. Harmison, one of our directors, has previously provided consulting services to Recom under a three-year agreement dated February 14, 2003. Under this agreement, Dr. Harmison provides advice in the areas of technological support and strategy, product development, medical and scientific advisory board development, and FDA regulation. We are obligated to pay Dr. Harmison $36,000 per year over the term of the agreement, payable quarterly. Dr. Harmison also received upon execution of the agreement an initial grant of options entitling him to purchase 216,000 common shares, in two tranches of 108,000 options, (36,000 shares pre-split) at $0.97 per share, exercisable over five years. The first tranche of 108,000 options vested immediately and the second tranche of 108,000 options vests over three years on a quarterly basis. Dr. Harmison is also entitled to receive (1) options exercisable into common shares in tranches of 20,000 shares per milestone for assisting Recom in attaining various milestones determined by our Board of Directors, including the preparation and filing with the FDA of a 510(k) application for our model 100 monitor product, approval of that application by the FDA, and market launch of that product; and (2) a grant of 20,000 common shares in the event of a change in control as that term is defined in the agreement. In the event the agreement is terminated by Recom for any reason other than negligence, misconduct, breach of its material terms by Dr. Harmison or the failure of Dr. Harmison to render services in a reasonable fashion, all compensation prospectively payable under the agreement will become due and payable in 90 days. .

We lease our principal office facilities, consisting of approximately 3,550 square feet and encompassing four suites including our administrative offices and research and development/laboratory facilities, through August 31, 2005. We may terminate the lease upon 30 days notice and the payment of two months rent. We currently pay approximately $8,600 per month in base rent for these facilities, which we believe reflects market value, and are also required to pay our share of any increase in operating expenses after August 2002. Operating expenses include expenses for maintenance of common areas, heating, air conditioning, plumbing, trash disposal, janitorial and security services and other like expenses.

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**LEGAL PROCEEDINGS**

On May 19, 2004, a complaint was filed against Recom in the Superior Court of Arizona, County of Maricopa, in an action entitled *William A. Miller v. Recom Managed Systems*. The complaint seeks declaratory relief, specific performance or damages for breach of contract. Mr. Miller alleged he was granted options to purchase 300,000 common shares of Recom at $0.01 per share. Recom believes the claim is without merit and plans to vigorously defend itself in the action. Prior to the filing of the complaint, none of the officers or directors of Recom had ever met with or spoken to Mr. Miller or his agents or even knew who Mr. Miller was. In July 2004, Recom filed a motion to dismiss the action on the basis of lack of personal jurisdiction, and is waiting for the court to set a hearing date for the motion. As of December 31, 2004, no amounts have been recorded as we believe that the likelihood of a negative outcome is not probable.

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**13.**

**SUBSEQUENT EVENTS**

On January 3, 2005, we granted to our directors as compensation for serving on our audit and compensation committees share five-year purchase warrants entitling them to purchase a total of 35,000 common shares at $5.05 per share. These options vest quarterly over one year.

On January 26, 2005 Recom filed, and on February 14, 2005 the SEC declared effective, a registration statement on form SB-2 covering, among other securities, the resale of common shares issuable to DKR SoundShore Oasis Holding Fund Ltd. upon conversion of principal or interest under their $2,000,000 8% convertible debenture. Under the terms of the debenture, once this registration statement is declared effective, Recom will have the right to repay both principal and interest in common shares in lieu of cash so long as we are not otherwise in default under the debenture. See Note 8, *Convertible Debenture Payable* .

Effective February 1, 2005, Recom approved the grant of common stock purchase options to seven non-executive employees entitling them to purchase a total of 92,000 unregistered common shares at an exercise price of $4.05 per share, representing the market price for the shares as of date of approval and grant. These options vest quarterly over a period of four year based upon the continuous provision of services and lapse, to the extent not exercised, on January 31, 2010.

On February 9, 2005, Recom approved the grant of a common stock purchase warrant to Lomond International, Inc. or its assigns that would entitle it to purchase a total of 500,000 unregistered common shares at an exercise price of $2 per share. The warrant would be granted as compensation for the provision of business advisory services in developing strategic relationships for our heart monitoring products with medical device market leaders. The warrant has not yet been issued and negotiations are continuing regarding its provisions and the services to be provided.

On March 3, 2005, Recom entered into a research and development services agreement. Pursuant to the agreement, we have agreed to pay labor services and other expenses for performance under the agreement, estimated at $2,815,200. The term of the services to be provided is estimated to be sixteen months. Services provided will be invoiced monthly. Either party shall have the right to terminate the agreement upon 30 days written notice for any good-faith basis.

On March 26, 2005, Recom appointed Dr. Lowell T. Harmison as our new Chief Executive Officer in replacement of Mr. Marvin H. Fink. On March 28, 2005, Mr. Harmison replaced Mr. Fink as President. The board of directors recognized the valuable services provided to the company by Mr. Fink and acknowledged to Mr. Fink that any common share purchase options he holds by reason of serving as an officer or director of the company shall be deemed fully vested by reason of those pre-retirement services. For similar reasons, the board of directors acknowledged on March 22, 2005 that Mr. Fink should be entitled to all other benefits under his employment agreement as if the contract had been lawfully and properly carried out by all parties to its full term.

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**SIGNATURES OF EXECUTIVE OFFICERS**

In accordance with Section 13 or 15(d) of the Exchange Act, the registrant caused this annual report on form 10-KSB to be signed on its behalf by the undersigned, thereunto duly authorized on March 28, 2005.

**RECOM MANAGED SYSTEMS, INC.**

By:

*/s/ Lowell T. Harmison*

Lowell T. Harmison,
Chief Executive Officer
(principal executive officer)

By:

*/s/ Robert C. Scherne*

Robert C. Scherne
Interim Chief Financial Officer
(principal accounting and financial officer)

**SIGNATURES OF BOARD OF DIRECTORS**

In accordance with the Exchange Act, this annual report on form 10-KSB has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

By:

*/s/ Lowell T. Harmison*

March 28, 2005

Lowell T. Harmison

Chief Executive Officer and Director

By:

*/s/ Lucy Duncan-Scheman**

March 28, 2005

Lucy Duncan-Scheman

Director and Chairman of the Board

By:

*/s/ Rodney Hildebrandt**

March 28, 2005

Rodney Hildebrandt

Chief Operating Officer and Director

By:

*/s/ Ellsworth Roston**

March 28, 2005

Ellsworth Roston

Director

By:

*/s/ Jennifer Black**

March 28, 2005

Jennifer Black

Director

By:

*/s/ Pamela Bunes**

March 28, 2005

Pamela Bunes

Director

* By:

*/s/ Lowell T. Harmison*

Lowell T. Harmison,

Agent-In Fact