

COMPREHENSIVE HEALTHCARE SOLUTIONS INC
Form 10KSB
June 15, 2005
UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, DC 20549

FORM 10-KSB

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

For the fiscal year ended February 28, 2005

Commission File Number: 003-08955

COMPREHENSIVE HEALTHCARE SOLUTIONS, INC.

(Exact name of registrant as specified in its charter)

Delaware

(State of other jurisdiction of incorporation or organization)

58-0962699

(IRS Employer Identification No.)

45 Ludlow Street, Suite 602, Yonkers, New York 10705

(Address of principal executive offices) (Zip Code)

(914) 375-7591

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(Registrant's telephone number, including area code)

(Former Address, since last report)

Securities registered pursuant to Section 12(g) of the Act:

Common Stock,
\$.10 par value

Name of each exchange on which registered. NASD OTC Bulletin Board

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding twelve 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. [X] YES [] NO

The aggregate market value of the outstanding Common Stock of the registrant held by non-affiliates of the registrant as of June 14, 2005, based on the average bid and asked price of the Common Stock on the NASD OTC Bulletin Board on said date was \$5,449,576.

As of June 14, 2005, the Registrant had outstanding 16,055,470 shares of common stock.

COMPREHENSIVE HEALTHCARE SOLUTIONS, INC.

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ITEM 1. BUSINESS

Directly, and indirectly through our subsidiaries, Accutone Inc. and Interstate Hearing Aid Service Inc., we are in the business of distributing and dispensing custom hearing aids. Accutone Inc. was formed under the laws of the State of Pennsylvania in October 1996 for the purpose of engaging in the manufacture, dispensing, and distribution of hearing aids. In 1998, Accutone acquired 100% ownership of Interstate, a Pennsylvania corporation and an FDA licensed hearing aid manufacturer which had been in the hearing aid business for approximately 35 years. In the Fall of 2000, Accutone discontinued all manufacturing operations and changed the focus of its marketing to be concentrated through Interstate Hearing Aid Service, Inc. to include, not only the individual, self-pay patients, but health care entities and organizations which could serve as patient referral sources for us. At that time, the hearing aid industry was competitively changing at a rapid pace. As a result management decided to identify additional business opportunities for substantial growth in various portions of the medical industry. Based on marketing research, management redirected its focus towards the 44 million plus uninsured and underinsured people throughout the United States.

To position ourselves to take advantage of this huge market, on March 1, 2004 pursuant to a Stock Purchase Agreement, we acquired one hundred percent (100%) of the issued and outstanding shares of common stock of Comprehensive Network Solutions, Inc. based in Austin, Texas from the CNS shareholders in consideration for the issuance of a total of 250,000 restricted shares of our common stock to the CNS shareholders. Pursuant to the Agreement, Comprehensive became our wholly owned subsidiary. Based on this acquisition, we changed our name to Comprehensive Healthcare Solutions, Inc. to better reflect the fact that we operate in several medical venues. This acquisition has positioned us to take full advantage of the opportunity to become a major player providing access to discounted health care provider networks and services.

History

Until the end of October 1999, when we discontinued all prior business activities, we produced and distributed popular priced branded fashion undergarments for sale, throughout the United States, to mass merchandisers and national chains. We produced and sold our men's underwear products primarily under licensed labels including Brittanica and Arrow and, until March 31, 1998, we also produced women's innerwear under the GUESS? label, for sale to department and specialty stores. From October 31, 1999 up to and including the period that we effectuated the reverse acquisition of Accutone and Interstate Hearing Aid we were a dormant corporation.

Subsequent to the reverse acquisition our only assets and business were those attributable to the acquired group of corporations. Until the summer of 2000, a small portion of our business consisted of manufacturing operations. However, because of changes in the competitive climate of the hearing aid manufacturing industry and the comparatively small level of our operations, all manufacturing was discontinued on July 30, 2000. This marked the beginning of an ongoing change in our revised business plan, which now encompasses concentrating our marketing to nursing homes, hospitals, out-patient clinics, members of managed health care providers, such as health maintenance organizations (HMO's), Physician Provider Organizations (physician group practices known as PPO's), union health plans, medicare, and medicaid while considering the expansion of an advertising campaign aimed at individuals in the non-insured self-pay market. Since implementing our revised business plan in October 2000, we have entered into contracts through Interstate Hearing Aid with approximately 65 managed health care provider organizations, unions, local municipalities and secondary health care insurance providers and pediatric care organizations in the New York metropolitan area, including Medicare and Medicaid. We are continually in negotiations with other such organizations and we anticipate that the number of such organizations will continue to grow. As a result of our additional marketing plan, changes and efforts, we have contracted with seven early intervention agencies. We have negotiated to sublease space in the offices of Early Achievers, Inc., an early intervention agency in White Plains, New York, with whom we have agreed to provide audiological early intervention services in exchange for the use of the space.

Upon receipt of the necessary capital as set forth herein, we also intend to execute a measured increase in our marketing activities aimed at individuals and managed health care organizations. We have also made positive strides and have been successful in identifying potential acquisition targets in medically related industries which we believe will add a material increase in gross revenues and profitability.

On March 1, 2004 pursuant to a Stock Purchase Agreement, we acquired one hundred percent (100%) of the issued and outstanding shares of common stock of Comprehensive Network Solutions, Inc. (CNS) based in Austin, Texas from the CNS shareholders in consideration for the issuance of a total of 250,000 restricted shares of our common stock to the Comprehensive shareholders. Pursuant to the Agreement, CNS became our wholly owned subsidiary. Additional consideration of \$60,000 was also paid to CNS to be used as working capital and we assumed a liability of \$25,000 for marketing services performed by an individual. Such liability was satisfied through the issuance of 25,000 shares of our restricted common stock to such individual. All shares issued in this transaction have a holding period of two years. Based on this acquisition, we changed our name to Comprehensive Healthcare Solutions, Inc. to better reflect the fact that we operate in several medical venues.

We estimate that in order to achieve our goals, many of which will involve the increase and expansion of marketing the Discount Medical Service Cards of our recently acquired, Comprehensive Network Solutions, Inc. Although there can be no guarantees of successfully attaining these goals, management will be actively pursuing same. We will require financing from sources other than cash flow, within the next six to eighteen months, in an amount ranging from \$1,000,000 to \$2,000,000. Our present plan for financing focuses on raising funds through a private placement of our securities. Although we have had some success in raising private placement funds, our efforts have fallen short of our previous expectations and the capital required to operate and market the discount medical card increased capital requirements more than anticipated. Also the time frame for revenue generation from these activities has taken much longer than was originally anticipated. Although the capital markets have a perceived improvement, we are cautiously optimistic of our abilities to achieve these goals. Along these lines, we are continually and actively pursuing potential businesses alliances with privately held businesses in like and or compatible medically related industries. We believe that the addition of both sales volume growth and profitability will greatly assist us in successfully raising additional capital.

Overview

Hearing Aid Industry

We continue to believe and are reinforced by nationwide statistics that hearing loss is one of the most prevalent chronic health conditions in the United States, and that its incidence is on the rise. Hearing loss occurs when there is damage to the auditory system, possibly caused by heredity, aging, noise exposure, illness, trauma, and/or some medications. Some hearing loss is temporary and/or can be corrected with medical or surgical treatment. Other types of hearing loss can be effectively managed with hearing devices. Although hearing loss traditionally has been considered an old person's condition, in several reports, the Better Hearing Institute reported that hearing loss is becoming increasingly common among the Baby Boomer 40 to 65 year old segment of the population. This is widely believed to be the result of extreme noise exposure, possibly because of a history of excessive exposure to extremely high decibel rock-and-roll concerts and the widespread use of walkman type radios (which produce a concentrated level of noise in extremely close proximity to the ear). The degree of hearing loss is often directly related to the amount of exposure and the intensity of loud noise. However, damaging noise does not necessarily have to result from extreme situations. Even cumulative exposure to everyday noises, such as the sounds of daily traffic, construction work, or a noisy office can contribute to hearing loss.

Hearing loss can have serious implications, leading to communication disorders, isolation, depression, cognitive dysfunction, and overall decline in quality of life. While hearing loss has historically been considered an effect of aging, recently some government agencies, health care organizations and insurance companies have begun increasing their scope of services and coverage's to include early interventions for children up to the age of 12. While a great many people suffering from hearing loss can be helped with the use of hearing aids, a survey by the National Council on the Aging (NCOA) indicated that older adults with hearing impairments, who do not wear hearing aids, are more likely to report sadness and depression, worry and anxiety, paranoia, diminished social activity, and greater insecurity than those who wear aids. We believe that the products and technologies currently available are broad and varied and in most instances can afford to the hearing impaired individual the amplification necessary to afford them the ability to have improved hearing and enjoy a full and normal lifestyle. In addition, we believe that these people could also benefit from the use of other assisted listening devices, such as telephone or television amplifiers (see Products, below).

The Future of the Industry

While we recognize that in the past and still today, many members of the public have been reluctant to use hearing aids, we believe that this industry can be expected to experience substantial and continuing growth during the coming decades. Management recognizes our ability to take advantage of these increases and that we must have required additional capital and infrastructure to be successful. Although the statistics of the last three years have shown minor growth, Sergei Kochkin, PhD, an officer and board member of the Better Hearing Institute and a director of market development at Knowles Electronics, has written a market research article in which he concluded that, "With modern estimates of hearing loss ranging from 24 million to 28 million and hearing instrument penetration at only 21% to 22% historically, it is of interest to determine the extent to which the more than 20 million hearing-impaired individuals who do not use hearing instruments are, in fact, current or future candidates for hearing aids. In the past we have conservatively estimated that if even 25% of the non-owner market were convinced to purchase hearing aids over the next five years that the market would double and retailers would realize an incremental \$1 billion a year."

Some of the factors which we believe will contribute to a measured expansion of hearing aid use and audiological services include the following:

- A rapidly aging population (the "graying of America") accompanied by a natural, progressive deterioration in hearing acuity;
- Wide exposure to excessive noise, pollution among younger segments of the population resulting in ever increasing damage to hearing;
- A growing acceptance among all segments of the population of the use of hearing aids;
- The availability of smaller and less visible hearing aids;
- Advances in hearing aid technology, including computerized digital products;
- Decreasing prices of hearing aids;
- Increasing coverage of hearing aid products by HMOs, PPOs, unions, employer sponsored groups, and Medicare and Medicaid to offset the costs to the end user; and
- Substantial increase in testing of pediatric patients since the medical profession has become aware of hearing losses in infants and toddlers.

As a result of the increase in the early intervention area of audiology, many health care organizations, managed care organizations and health care insurance companies (including Medicaid) have begun to reimburse the costs of implementing early intervention testing procedures in their reimbursement schedules. We are currently expanding our marketing efforts in the early intervention segment of our business, mainly through the efforts of John H. Treglia our Chairman and CEO.

Our Sales and Dispensing Offices

We are currently operating three hearing aid sales and audiological testing facilities. These are retail sales and dispensing offices, which are located in medical arts buildings, independent office space in a professional type office building, and, in one case, on-site at a medical outpatient center. One of our retail offices is located in Yonkers, New York, one is in Mount Vernon, New York, and one is in Forty Fort, Pennsylvania. Our Mount Vernon facility is located on-site at The Wartburg Home of The Evangelical Lutheran Church in its 16,000 square foot outpatient facility.

Our Yonkers office and our Pennsylvania office are open and functioning on a full time basis. Our Wartburg out-patient office is currently open two days per week and our Wartburg Nursing Home office is currently open an average of four days per month, on an as-needed basis. Our Ludlow Street Yonkers office is staffed and supervised by a full-time, licensed and certified audiologist and one full-time patient care coordinator. Our Pennsylvania office operates on a full time basis and is staffed by a state licensed hearing aid dispenser, as required by applicable Pennsylvania law and at least one clerical employee.

Our current New York sales and dispensing offices range from 600 to 1,100 square feet in size. These include our Yonkers office and our on-site Wartburg Outpatient Facility office, all of which are fully equipped with:

- * soundproof testing booths and state-of-the-art testing equipment that meets or exceeds all state standards; and

- * a full range of diagnostic and auditory-vestibular tests that assist referring physicians in the treatment of patients with hearing and balance disorders.

Our on-site nursing home offices, which do not have their own existing on-site testing booths and audiological equipment, are equipped with our portable electronic audiological equipment brought in by the audiologist at each visit. This equipment meets or exceeds the requirements of all federal and state agencies as well as all third-party payers. We have found this equipment to be adequate to serve the needs of almost all patients at these facilities and continually upgrade all equipment to the latest industry standards.

On-Site Offices

The Wartburg Adult Care Community Outpatient Clinic and The Wartburg Nursing Home

We have entered into lease and service agreements with The Wartburg Adult Care Community Outpatient Clinic and the Wartburg Nursing Home. These facilities are part of the Wartburg Adult Care Community which is located in a 36-acre campus in the town of Mount Vernon in Westchester County, New York. The Wartburg is a comprehensive senior health care complex which includes residential assisted living, nursing home, and critical care facilities as well as a 16,000 square foot Outpatient Health Services complex serving area residents as well as persons residing within the Wartburg facilities. Our contracts with the outpatient clinic and the nursing home provide for our:

- * Operating an on-site dispensing and testing office in the Wartburg Diagnostic and Treatment Center (outpatient center). Under the terms of the contract, our office has use, at no cost, of a common reception and waiting room and reception personnel in the Wartburg, who will schedule and coordinate patient appointments. This facility is fully equipped, including a sound-proof booth, and all required electronic testing equipment as well as all other peripheral equipment necessary for appropriate audiological testing and the fitting and dispensing of hearing aids. This office is used for the treatment of both non-resident outpatients and Wartburg assisted living facility residents. We are currently in the process of expanding the patient base to include early intervention (pediatric testing and evaluation) as well as dispensing of hearing aids when deemed appropriate and necessary.

- * Operating a separate on-site dispensing and testing facility in Wartburg nursing home (The Wartburg Home of the Evangelical Lutheran Church, Inc.). Wartburg provides treatment and waiting room areas within the nursing home to be used

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as an audiological testing, fitting, and dispensing facility for its nursing home patients, utilizing portable and mobile, state of the art, testing and fitting equipment.

Presently, the Wartburg outpatient facility handles six hundred patient visits per month. We had anticipated that during the past six months, we would devote a total of approximately two to three days per week to patients at the Wartburg facilities, but we fell short of our expectations. The Wartburg Diagnostic and Treatment Center had advised us that it intended to actively promote its outpatient services but financial constraints have prohibited them from doing so. We will continue to expand our own marketing program as soon as the financial resources are available to us. We intend to coordinate such a marketing program with the Wartburg so as to maximize promotion of our Wartburg outpatient facility, as well as our other facilities. Because of financial constraints, the Wartburg was unable to fully implement its projected marketing program. This has continued to negatively impact our projected growth of our audiological services and hearing aid sales. It is our belief that our continued coordinated marketing efforts and the physical presence of our facility on-site, will increase patient awareness of our services. To date, we have not been as successful in our business operations as our original projections had lead us to believe. With

anticipated increases in capital and fording, we continue to believe these goals of additional revenues and/profitability can be attained. In response to the expected growth in pediatric and early intervention services which are to be added to those services we already provide, the Wartburg is in the process of constructing 2 separate waiting rooms for its patients. It is intended that one room will be for seniors and one will be for pediatric patients.

This construction is not being undertaken solely to accommodate our patients but also for the Wartburg's expected entrance into pediatric medical, psychiatric and physical rehabilitation services. As a result, we intend to increase our personnel and operating hours at the Wartburg Out-Patient Clinic in order to adequately service the non-resident outpatients that will be added, as well as the full time residents/patients of the facility.

Existing Contracts with Nursing Home Facilities

We have presently entered into contracts with approximately forty two nursing homes for the establishment of on-site offices and our appointment as sole provider of audiological services and products during the terms of the contracts.

In the past we had aggressively pursued contracts with new nursing home facilities (especially those that have been made available to us pursuant to the needs of our association with Park Avenue Medical Associates, PC as set forth herein). However, we have currently curtailed these efforts due to capital constraints which prevent us from adding to our professional staff of audiologists and therefore adding to the number of nursing home and senior care facilities we are currently unable to service.

We are also in process of renegotiating existing contracts with these facilities to add additional revenues to make up for the cuts in Medicaid and Medicare reimbursement rate. If we are unsuccessful in renegotiated these rates to provide the company with additional sales and profitability, we may consider curtailing services to some of these nursing homes.

Contract With Park Avenue Health Care Management Inc.

On February 15, 2002, we executed an Agreement with Park Avenue Health Care Management Inc. and its affiliate, Park Avenue Medical Associates, P.C.(referred to herein, collectively, as Park Avenue) which closed on February 28, 2002. Pursuant to this Agreement, Park Avenue contributed its entire Audiology business in consideration for the issuance of 1,200,000 of our shares to Park Avenue. Park Avenue is a health care management organization which services nursing homes, hospitals, assisted living facilities, adult day care centers, adult homes, and senior outpatient clinics. Park Avenue directly employs medical professional personnel, including physicians in both general and specialty practices and other health care professionals such as podiatrists, audiologists, and optometrists.

Nursing homes contract with Park Avenue for the services of its medical professionals, on a pre-determined schedule or on an as-needed basis. Park Avenue presently provides staff to approximately seventy-two nursing homes. We anticipate that with additional operating capital we will be able to service a majority of these nursing homes and senior care facilities.

Our Services

We provide all of our patients at our retail, nursing home, and out-patient clinic sales and dispensing offices with comprehensive hearing care services consisting of the following:

- an interview with one of our audiologists or patient care coordinators respecting the hearing problems and all factors which may contribute to or cause such problems;
- an internal and external examination of the patient's ear performed by one of our audiologists;
- an initial hearing screening to establish a permanent base-line hearing acuity and to determine whether the patient has a hearing problem;
- if the initial screening indicates that there is a hearing problem, the audiologist will then perform additional testing and do a complete

audiological evaluation, including:

- * air conduction;
- * bone conduction;
- * speech recognition thresholds;
- * most comfortable hearing level;
- * uncomfortable hearing level;
- * site of lesion tests, if required;
- * tympanometry;
- * acoustic reflex testing; and
- * acoustic reflex decay.

The patient is then counseled with respect to the results of the audiological testing and evaluation, the nature and extent of any hearing defects found, the possible effects of such hearing aids on the patient's lifestyle, and the options for treatment with a hearing aid; and if it is determined that a hearing aid would be of benefit to the patient, an appropriate aid will be prescribed and fitted; the fitting process will include taking impressions of the affected ear or ears.

All hearing aids that we prescribe are custom made for the individual patient. Delivery is usually made within one week to ten days. When the patient receives the hearing aid, the audiologist explains the properties and capabilities of the hearing aid, and demonstrates proper insertion, removal, maintenance techniques, and the operation of all the features of the hearing aid. The patient is then re-tested wearing the hearing aid to enable the audiologist to determine whether the hearing aid is performing to prescribed standards and to evaluate the benefit to the patient. After one week, the patient care coordinator will contact the patient by telephone to discuss any problems or questions and to schedule a follow-up appointment if the patient or the patient care coordinator feels it is needed.

We provide follow-up services including, where necessary, additional personal contacts with the patient and/or the patient's family, for the purpose of monitoring and guiding the patient's progress in successfully utilizing the hearing aid and making all adjustments required to insure a successful outcome. We also have a family hearing counseling program to help the patient and his or her family understand the proper use of their hearing products and the nature of their disability. These services are provided on an as needed basis as determined by the licensed audiologists.

In addition to all of the foregoing services, at the Wartburg Nursing Home, and at all on-site offices which we may establish at other nursing homes in the future:

- * We continually coordinate with these facilities for the payments which have not been reimbursed by the various third party payors and are to be paid to us by the facilities or the patients (this does not include Medicaid beneficiaries).
-

- * we work directly with the director of the facility and nursing staff to insure that all residents and patients are provided any required audiological assistance on a timely basis.

- * patient s appointments are scheduled by the nursing home personnel at intervals of approximately one-half hour to forty-five minutes;

- * all patients are seen at the direction and referral of his or her ear nose and throat specialist or primary care physician;

- * we provide base-line hearing screening for all new admissions including residents and short-term rehab patients; and

- * results of all procedures are reported to the attending physician and become a part of the patient s permanent medical records.

Early Intervention Services

While hearing loss has historically been considered an effect of aging, recently health care professionals as well as some government agencies, healthcare organizations and insurance companies have begun to increase their scope of services and coverage s to include early interventions for infants and children up to the age of 16. The reason for the rise in early intervention is due to the fact that many organizations now believe that pediatric hearing impairment may be the cause, or part of the reason, for such disorders as Attention Deficit Disorder, Dyslexia, disciplinary problems, educational underachievement and disfunctional behavior with a family setting, especially with siblings. Unfortunately, many of these problems have been deemed to be caused by alcohol and drug abuse by the child s mother or other prenatal problems which were not previously brought to light. We currently have referral contracts with and provide audiological services to the following agencies:

- First Step Services, Inc.
- Los Ninos Community Services
- Speech and Communications Professionals
- Project Rainbow
- Secundino Services, Inc
- Early Achievers Services, Inc.*
- Paxxon Healthcare Services, LLC

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* We have negotiated to utilize space in the offices of Early Achievers, Inc., an early intervention agency in White Plains, New York,. We have agreed to provide audiological early intervention services at a reduced rate of compensation in exchange for the use of the space as well as their continuing to refer all of their early intervention patients to our company.

As a result of our providing such services for these companies, we are continually approached by similar organizations and we believe that we can attain growth in this potential source of additional revenues to our company if our operating capital improves.

Our Products

A hearing aid is an electronic, battery-operated device that amplifies and transforms sound to allow for improved communications. All hearing aids consist of three components: the microphone, the amplifier, and the loudspeaker. Sound is received through the microphone, which vibrates in response to sound waves and converts the sound waves to electrical signals. The amplifier enhances the intensity of these signals before transmitting them to the loudspeaker where they are converted back to sound waves for broadcast in the ear.

All hearing aids that we prescribe are custom made for the individual patient. We have selected a variety of major worldwide manufacturers products, to make available through our offices, in order to provide the best possible hearing aid products for our patients. These include the latest digital technology available from Magnatone, Siemens, Phonak, Sonotome, Lori/Unitron, United Hearing Systems, and others. We are also able to make available, by special order, a large selection of other hearing enhancement devices including telephone and television amplifiers, telecaptioners and decoders, pocket talkers, specially adapted telephones, alarm clocks, doorbells and fire alarms.

Customers

To date, we have continued to expand our patient referral base by securing our appointment as the potential sole providers of hearing aids and audiological services to nursing homes, out-patient facilities, and adult group homes with whom we have contractual arrangements. We have also established relationships and have signed contracts with other types of health care organizations, such as HMO's and PPO's. Our affiliations with these types of health care organizations and facilities have grown rapidly to the extent that our current capital structure has allowed.

Existing Contracts With Health Care Providers and Third-Party Payers

To date we have entered into contracts for the provision of audiological services with an excess of sixty health care provider organizations, as well as third-party payers such as Medicare and New York State Medicaid. We expect these additional contracts to continue to grow as we progress. We believe that we currently have sufficient staff and facilities which are geographically accessible for all participants in organizations which we have contracted with.

In general, our agreements with health insurance or managed care organizations provide for services to be offered on four different bases, including:

- (1) fee for service basis based on a contractual rate which we offer to provider's members (all paid for by the patient); and
- (2) an encounter basis where we are paid a fixed fee by the insurance or managed

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care organization for each hearing aid sold (with the balance paid to us by the individual member).

- (3) a special Medicare/Medicaid encounter basis where we are paid a fixed fee by Medicare and/or Medicaid for particular audiological services, at a price pre established by Medicare or Medicaid (other than the deductible amount, which is paid either by the patient or other third-party payers).
- (4) For those services not covered by a third party payor to be paid either by the facility or the patients family members.

Requirement for Renewal of Agreements with Health Insurance and Managed Care Organizations

The terms of most agreements with health insurance and managed care organizations are subject to renegotiation annually. Moreover, most of these agreements may be terminated, at any time, by either party on 90-days notice. Even if we are successful in expanding our base of contracts with such organizations and institutions, the early termination or failure to renew such agreements could adversely affect our results of operations. To date, we have not been terminated and, in some instances, new and updated contracts have been signed.

Nursing Homes

Approximately fourteen nursing homes, assisted living facilities and adult daycare centers currently provide out-patient referrals and transportation of their residents to our Ludlow Street office. We also provide limited on-site testing and evaluations within these nursing homes for residents who are disabled or infirm.

Existing Referral Arrangements With Out-Patient Facilities

We have established relationships with four local out-patient facilities and these referrals continue to steadily increase. We had believed that patient referrals from these sources would continue to grow based upon the positive feedback we receive from these out-patient facilities, but we have been unable to realize these goals.

On-Site Offices

We have established an on-site office at The Wartburg Adult Care Community Outpatient Clinic, where our location makes us the sole on-site audiological services provider to patients being treated at the clinic. We have also established an on-site office at The Wartburg Nursing Home where we are the exclusive provider of audiological services to all residents at the Nursing Home. Our audiologist visits the out-patient clinic two half-days per week and the nursing home four half-days per month. On average, our audiologist sees approximately six to eight patients, per half-day, at each of these facilities.

Area Hospitals

We have established relationships with five area hospitals who have been referring patients to our Ludlow Street office. The hospitals with which we have established patient referral relationships are:

1. Saint Josephs Medical Center South Yonkers, NY
2. Yonkers General Hospital South Yonkers, NY
3. Montefiore Medical Center Northeast Bronx, NY
4. Westchester Medical Center White Plains, NY
5. Saint Johns Medical Center

Physician Referrals

Referrals from physicians are generally based upon personal contacts and established patient and physician satisfaction. We endeavor to maintain our relationships with referring physicians by using a timely comprehensive medical reporting system which provides each referring physician with a full audiological report on each of their patients that visit our offices.

Payments for Services

Our customer base includes self-pay patients, patients whose costs are covered by medicare or medicaid, patients whose costs are covered by private health care organizations; and patients whose costs are covered as union benefits). Treating Medicare and Medicaid patients involves payment lag issues which are currently problematic for us because of our current capital constraints. Current Medicare and Medicaid payments for audiological services and hearing aids can take as long as 120 to 180 days after approved services are provided and hearing aids are dispensed. An additional recent disadvantage to servicing Medicare and Medicaid patients resulted from the cut in reimbursement rates from both agencies. In order to assist us with the cash flow lag, we have been successful in obtaining from some of our suppliers an extension of their normal payment term. We are hopeful that if the current domestic economic conditions improve in the near future, we will be able to put bank financing arrangements into place which will provide us with a credit line for working capital.

Sales and Marketing

Recognizing that there is still a vast untapped market of hearing impaired individuals, we intend to continue to expand our marketing efforts to include, on a more highly concentrated basis self-pay patients who had previously not been our principal customer base, to include:

- physicians in private or group practices;
 - providers of group health care;
 - unions;
 - nursing homes;
 - senior care facilities;
 - out-patient health care clinics;
 - hospitals;
 - speech pathology groups;
-
- nursing home managed
 - health care organizations; and
 - third party payers, including Medicare and New York State Medicaid.

Marketing to these organizations and entities has consisted and for the near foreseeable future solely of personal contacts by our CEO, John H. Treglia, with all of the types of entities and organizations listed above.

Proposed and Existing Advertising and Marketing Program

We intend to continue to try to bring our company and our services and products to the attention of managed care providers, which can promote our products and services to the hearing impaired, and to their participating members. We also intend to increase our marketing efforts to the self-pay, (uninsured patient) market when sufficient operating capital is made available. Our marketing plan contemplates implementing an aggressive advertising and marketing program focused on both of these markets, highlighting the quality of our services and products, as well as competitive pricing. In addition, to address the substantial growth in the number of assisted living facilities and nursing homes, we intend, when financial resources are available, to retain a director of senior care and nursing home marketing to promote and develop relationships with such establishments. At present, all marketing to health care organizations is done by our CEO, John Treglia. Our marketing and advertising efforts have been continually hindered by our capital constraints which have adversely effected our originally projected higher gross profit percentages.

Business Strategy - Audiological Services

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Our original business plan recognized that increasing the number of our sales offices would make our services conveniently accessible to a greater number of participating members of health care organizations and other entities with which we have relationships or may establish relationships. Our original plan was intended to couple such an increase in offices with an expansion of our patient referral base. We expected this two-pronged approach to enable us to substantially increase the volume and profitability of our business by further concentrations on the private pay population. Although we intend to maintain the audiological services currently offered, our original expansion plans for this segment of our business have been curtailed in order to focus our efforts and capital on our Medicare discount Card operations.

Dependence on Outside Manufacturers of Hearing Aids

We currently make available to our customers hearing aids supplied by approximately seven major manufacturers, as well as hearing enhancement devices manufactured by other companies. There are currently approximately 40 manufacturers of these products world wide and few manufacturers offer dramatic product differentiation. We are therefore confident that, in the event of any disruption of supply from any of our current sources, we could obtain comparable products from other manufacturers on comparable terms. We have not experienced any significant disruptions in supply in the past.

Dependence on Qualified and Licensed Audiological Personnel

We employ New York State licensed, ASHA certified audiologists in our New York offices. In our Pennsylvania office and in-home services, Registered Hearing Aid Fitters provide primary services, with licensed audiologists available on a consulting basis. In our New York area operations, we currently have two full-time, and one part-time, New York State audiologist. In our Pennsylvania operation, we have four available Registered Hearing Aid Fitters in Pennsylvania, who are employed by us, on a part-time basis, as independent contractors, and two Pennsylvania licensed audiologists available on a consulting basis for special needs.

Should we be unable to attract and retain qualified audiologists or Registered Hearing Aid Fitters, either as employees or independent contractors, it could limit our ability to compete effectively against competing hearing aid retailers and thus adversely affect our business. There are currently 6,000 audiologists in the United States and approximately 200 educational institutions in the United States which offer audiology degree/certification programs. There is currently a shortage of qualified personnel in the industry which could potentially cause us to encounter problems attracting and retaining sufficient audiological staff, and cause us to be at a competitive disadvantage against larger, better financed, and more well-established hearing aid providers for the services of qualified personnel.

Government Regulation

Federal

The practice of audiology and the dispensing of hearing aids are not presently regulated on the Federal level. The United States Food and Drug Administration(FDA) is responsible for monitoring the hearing care industry. Currently there are only two regulations affecting the sale of hearing aids:

- (i) A physician's review. While the FDA requires first time hearing aid purchasers to receive medical clearance from a physician prior to purchase, patients may sign a waiver in lieu of a physician's examination. A majority of our patients and targeted market are members of the managed care or institutional providers with whom we have

contracts, or whom we expect to enter into contracts with, to provide hearing care.

Some of these organizations require a physician referral. Consequently, even if any new federal or state physician referrals are mandated in the future, they should not be expected to have an adverse impact on our operations.

- (ii) A return policy. The FDA requires states to adopt a return policy for consumers offering them the right to return their products, generally within three to forty five- days. In Pennsylvania, where the state mandated return period is three days, we offer our customers a full thirty-day return policy. In New York, the state requires a forty-five day return period, which we comply with. Moreover, if our audiologist determines that an individual patient requires additional time to become acclimated to using a hearing aid, we will extend the return period to accommodate such special needs.
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In addition, because we accept Medicare and Medicaid patients, each of our sales and dispensing offices must maintain their eligibility as Medicare/Medicaid providers and must comply with related federal anti-fraud, anti-kickback and other applicable regulations. Federal laws prohibit the payment of remuneration(kickbacks) in return for a physician referring a Medicare or Medicaid patient, and those laws limit physicians from referring patients to providers in which they have a financial interest. We believe that none of our managed care or other provider contracts or our relationships with referring physicians are violative of the anti-kickback statute.

We are unable to predict the effect of future changes in federal laws, or the impact that changes in existing laws or in the interpretation of those laws might have on our business. We believe we are in material compliance with all existing federal regulatory requirements.

State

Generally, state regulations, where they exist, are concerned primarily with the formal licensure of audiologists and of those who dispense hearing aids and with practices and procedures involving the fitting and dispensing of hearing aids. In Pennsylvania and New York, where we currently operate, and in New Jersey and Connecticut, which are part of our currently targeted markets, such regulations do exist. We believe we are in compliance with all applicable regulations in Pennsylvania and New York and we intend to format all of our programs in Connecticut and New Jersey so that they are in full compliance with the regulations of those states. While we believe it is unlikely, there can be no assurance that regulations will not be promulgated in states in which we operate, or plan to operate, which could have a material adverse effect upon us. Such regulations could include stricter licensure requirements for dispensers of hearing aids, inspections of centers for the dispensing of hearing aids and the regulation of advertising by dispensers of hearing aids. We know of no current or proposed state regulations with which we, as we currently operate, could not comply.

Product and Professional Liability

In the ordinary course of our business, we may be subject to product and professional liability claims alleging the failure of, or adverse effects claimed to have been caused by, products sold or services which we have provided. We maintain insurance at a level which we believe to be adequate. Each of our licensed audiologists is also required by state law to carry appropriate malpractice liability insurance. All of our audiologists have furnished us, as well as all nursing homes, assisted living, adult day care, senior care, HMO s, PPO s and other managed care organizations with whom we have contractual or other relationships with copies of their insurance coverage certificates. As apart of this process we also keep records of all license and insurance anniversary and/or effective dates to attempt to insure compliance. We believe that they are all in compliance with applicable federal and state requirements. Also included as a part of compliance with the credentialing requirements, copies of all educational degrees, certificates and licensing are appropriately maintained. While we believe that it would be highly unlikely that a successful claim would be in excess of the limits of our insurance policies, if such an event should occur, it could conceivably adversely affect our business. Moreover, because we distribute products manufactured by others, we believe we will have recourse against the manufacturer in the event of a product liability claim. It should be noted however that we could be unsuccessful in a recourse claim against a manufacturer or, that even if we were successful, such manufacturer might not have adequate insurance or other resources to make good on our claim.

Competition

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The hearing care industry is highly fragmented with approximately 11,000 practitioners providing testing and dispensing products and services. Approximately 2,500 of these practitioners are audiologists working for hospitals or physicians, 2,500 of the practitioners are licensed audiologists in private practice, and the remaining 6,000 are hearing aid specialists. Industry surveys estimate that approximately 5% of all hearing aids are sold in physicians' offices, 60% are dispensed by qualified audiologists in private practice, and the remaining 35% are sold by hearing aid specialists.

Because there are no federal, state or local regulatory or oversight agencies in the hearing care industry, it is not possible to determine the precise number of competitors in every market which we are operating in or which we intend to enter. Our present plan is to continue to focus our efforts primarily on urban, high density population areas, since we believe these areas will best implement our current business plan and potential growth with a minimal amount of impact on our current capital structure.

Although the hearing care industry is largely fragmented and to date there have been few successful efforts to consolidate the establishment of coops and alliances, the trend in this area has been greatly accelerated, and we feel that the amount of competition both in pricing and services offered may greatly increase.

There are however networks which are owned by companies having greater resources than are available to us, and there can be no assurance that one or more of these competitors will not expand and/or change their operations to capture the market targeted by us. Nor can there be any assurance that the largely fragmented hearing care market cannot be successfully consolidated by the establishment of co-operatives, alliances, confederations or the like which would then compete more effectively with us in our intended market areas.

Employees

As of June 14, 2005, in our New York area operations, we had a total of four full-time, and two part-time employees. Full-time employees include, our CEO, John H. Treglia, two New York State licensed audiologists, and one receptionist - patient care coordinator. In our Pennsylvania operations, we employ two full-time employees. Our part-time employees consist of three Pennsylvania Registered Hearing Aid Fitters, who work for us, on an as needed basis (part- time), and two Pennsylvania licensed audiologists who consult with us on an as needed basis.

Medical Discount