

VASOMEDICAL INC
Form 10-KT
April 30, 2012

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, DC 20549

FORM 10-K

ANNUAL REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the fiscal year ended _____
 TRANSITION REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from June 1, 2011 to December 31, 2011
Commission File No. 0-18105

VASOMEDICAL, INC.
(Exact name of registrant as specified in Its Charter)

Delaware 11-2871434
(State or other (IRS
jurisdiction of Employer
incorporation or Identification
organization) No.)

180 Linden Avenue, Westbury, New York 11590
(Address of Principal Executive Offices) (Zip Code)

Registrant's telephone number, including area code: (516) 997-4600
Securities registered under Section 12(b) of the Act: None
Securities registered under Section 12(g) of the Act:

Common Stock, \$.001 par value _____ OTCQB
(Title of Class) Name of each exchange on which
registered

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act.

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 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 No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files)

Yes No

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Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§229.405) is not contained herein, and 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-K or any amendment to this Form 10-K. [X]

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. Large accelerated filer [] Accelerated filer [] Non-accelerated filer [] Smaller reporting company [X]

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

The aggregate market value of common stock held by non-affiliates was approximately \$23,729,000 based on the closing sales price of the common stock as quoted on the OTCQB on April 23, 2012.

At April 23, 2012, the number of shares outstanding of the issuer's common stock was 158,682,110.

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- Exhibit 31 - Certifications Pursuant to Securities Exchange Act Rule 13A-14(A)/15D-14(A)
Exhibit 32 - Certification of Periodic Report

PART I

ITEM 1 – BUSINESS

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

General Overview

This Transition Report on Form 10-K is being filed for the seven months ended December 31, 2011 as a result of the Company’s decision to change its fiscal year end from May to December. Consequently, annual reports in the future will report on a calendar year basis.

Vasomedical, Inc. was incorporated in Delaware in July 1987. Unless the context requires otherwise, all references to “we”, “our”, “us”, “Company”, “registrant”, “Vasomedical” or “management” refer to Vasomedical, Inc. and its subsidiaries. In 1995, we have been engaged in designing, manufacturing, marketing and supporting EECP® Enhanced External Counterpulsation systems, based on our proprietary technology, to physicians and hospitals throughout the United States and in select international markets.

In 2010, the Company, through its wholly-owned subsidiary Vaso Diagnostics d/b/a VasoHealthcare, organized a group of medical device sales professionals and entered into the sales representation business as the exclusive representative for the sale of select General Electric Company (GE) diagnostic imaging equipment to specific market segments in the 48 contiguous states of the United States and the District of Columbia.

In September 2011, the Company acquired Fast Growth Enterprises Limited (FGE), a British Virgin Islands company, which, through its subsidiaries, owns and controls two Chinese operating companies - Life Enhancement Technology Ltd. and Biox Instruments Co. Ltd., respectively - to expand its technical and manufacturing capabilities and to enhance its distribution network, technology, and product portfolio. Also in September 2011, the Company restructured to further align its business management structure and long-term growth strategy, and now operates through three wholly-owned subsidiaries. Vaso Diagnostics d/b/a VasoHealthcare continues as the operating subsidiary for the sales representation of GE diagnostic imaging products; Vasomedical Global Corp. operates the Company’s newly-acquired Chinese companies; and Vasomedical Solutions, Inc. was formed to manage and coordinate our EECP® therapy business as well as other medical equipment operations.

We have achieved profitability through the operations of the VasoHealthcare business. The Company will seek to achieve greater profitability through our recent accretive acquisition of the two Chinese medical device companies and by expanding our U.S. market product portfolio. In addition, the Company plans to actively pursue other accretive acquisitions in the international market and is in preliminary discussions to secure a credit facility for up to \$25

million to be utilized for this purpose.

Business Segments

We manage and evaluate our operations based on the products and services we offer. Under this approach, we operate through two segments - Sales Representation and Equipment. Our principal manufacturing facilities are located domestically in New York, and internationally in China.

Sales Representation

The Sales Representation segment operates under a sales representative agreement with GE Healthcare (the “GEHC Agreement”), the healthcare business unit of GE, which commenced July 1, 2010. The GEHC Agreement has an initial term of three years, subject to extension and also subject to earlier termination under certain circumstances. All revenues and expenses in this segment arise through its operations under the GEHC Agreement.

Under the GEHC Agreement, the Company earns commissions based upon achieving certain calendar year targets. Our commission rate increases as targets are met, resulting in higher rates, should we meet our targets, as the year progresses. The progressive nature of our agreement can thus result in significantly higher commissions due us in the fourth and first quarters as compared to the second and third quarters of the calendar year.

The Company has been successfully meeting its obligations under the GEHC Agreement since inception.

Sales and Marketing

We sell diagnostic imaging products to our assigned market through a nationwide team of sales employees led by a vice president of sales and several regional managers, supported by in-house administrative and other support, as well as applicable GEHC employees.

Competition

In the U.S. diagnostic imaging market, our main competitors are Hologic, Philips, Siemens, and Toshiba. Key competitive factors in the market include price, quality, delivery speed, service and support, innovation, distribution network, breadth of product and service offerings and brand name recognition. We believe GEHC is a leading competitor in this market.

Equipment

The Equipment segment operates through two subsidiaries: Vasomedical Solutions and Vasomedical Global. The segment primarily designs, manufactures and distributes medical devices, including EECP® systems, ambulatory monitoring devices, and patient management devices. Vasomedical Solutions maintains a manufacturing facility in New York and markets EECP® therapy systems and other medical equipment both in the United States and in select international markets. Vasomedical Global currently operates engineering development and production facilities in China. In addition to being the primary supplier of medical equipment to Vasomedical Solutions, it also sells its ambulatory monitoring products directly to end users in China and other countries.

Market Overview - EECP®

Cardiovascular disease (CVD) is the leading cause of death in the world and is among the top three diseases in terms of healthcare spending in nearly every country. CVD claimed approximately 812,000 lives in the United States in 2008 and was responsible for 1 of every 3 deaths, according to The American Heart Association (AHA) Heart and Stroke Statistical 2012 Update (2012 Update). An estimated 82.6 million American adults suffer from some form of cardiovascular disease. Among these, 16.3 million have coronary heart disease (CHD).

We have FDA clearance to market our EECP® therapy for use in the treatment of stable and unstable angina, congestive heart failure, acute myocardial infarction, and cardiogenic shock; however, our current marketing efforts are mostly limited to the treatment of chronic stable angina and congestive heart failure. Medicare and other third-party payers currently reimburse for the treatment of angina pectoris patients with moderate to severe symptoms who are refractory to medications and who, in the opinion of a cardiologist or cardiothoracic surgeon, are not

candidates for invasive procedures. Patients with co-morbidities of heart failure, diabetes, peripheral vascular disease, etc. are also reimbursed under the same criteria, provided the primary diagnosis and indication for treatment with EECPC® therapy is refractory angina symptoms.

Angina

Angina pectoris is the medical term for a recurring pain or discomfort in the chest or near the neck due to coronary artery disease (CAD). The number of angina patients in the United States is approximately 9.0 million, according to the 2011 Update. There are approximately 100,000 to 150,000 new refractory angina patients each year who do not adequately respond to medication, and are not amenable to invasive revascularization procedures such as percutaneous coronary interventions (PCI), with angioplasty and coronary stent placement or coronary artery bypass grafting (CABG). Currently our EECP® therapy is mostly prescribed for these patients because of the potential to meet the guidelines for reimbursement of EECP® therapy.

In February 1999, the Centers for Medicare and Medicaid Services (CMS), the federal agency that administers the Medicare program for approximately 47.7 million beneficiaries in 2011, issued a national coverage policy for the use of external counterpulsation therapy in the treatment of refractory angina. Medicare reimbursement guidelines have a significant impact in determining the available market for EECP® therapy. We believe that the majority of the patients who receive EECP® therapy are Medicare patients, and many of the younger patients are covered by third-party payers. Medicare guidelines limit reimbursement for EECP® therapy to patients who do not adequately respond to medical therapy and are not readily amenable to invasive therapy. As a result, an important element of our strategy is to grow the market for EECP® therapy by expanding reimbursement coverage to include a broader range of angina patients than the current coverage policy provides and enable EECP® therapy to compete more with other therapies for ischemic heart disease. To this end, we have engaged a consulting firm in a two-year agreement to assist us in promoting EECP therapy as a first line option in the treatment of CCS Class III/IV angina with both Medicare and a major healthcare third-party payer, and extending Medicare coverage to heart failure and Class II angina. Please see the "Reimbursement" section of this Form 10-K for a more detailed discussion of reimbursement issues.

Congestive Heart Failure (CHF)

CHF is a condition in which the heart loses its pumping capacity to supply the metabolic needs of all other organs. The condition affects both sexes and is most common in people over age 50. Symptoms include angina, shortness of breath, weakness, fatigue, swelling of the abdomen, legs and ankles, rapid or irregular heartbeat and low blood pressure. CHF is treated with medication surgery, and, in certain severe cases, heart transplants. Left ventricular assist devices (LVADs) and the use of cardiac resynchronization and implantable defibrillators are useful in selected patients with heart failure. Still, no consensus therapy currently exists for CHF and patients must currently suffer their symptoms chronically and have a reduced life expectancy.

According to the 2012 Update, in 2008 approximately 5.7 million adults in the United States were suffering heart failure and about 670,000 new cases of the disease occur each year. The prevalence of the disease is growing as a result of the aging of the population and the improved survival rate of people after heart attacks. Because the condition frequently entails visits to the emergency room and in-patient treatment centers, two-thirds of all hospitalizations for people over age 65 are due to heart failure. Congestive heart failure offers a good strategic fit with our current angina business and offers an expanded market opportunity for EECP® therapy. Unmet clinical needs in CHF are greater than those for angina, as there are few consensus therapies, invasive or otherwise, beyond medical management for the condition. It is noteworthy that data collected from the International EECP® Patient Registry™ (IEPR) at the University of Pittsburgh Graduate School of Public Health shows that approximately one-third of angina patients treated with EECP® also have a history of CHF and 70% to 80% have demonstrated positive outcomes from EECP® therapy.

We will continue to educate the marketplace that EECP® therapy is a therapy for ischemic cardiovascular disease and that patients with a primary diagnosis of heart failure, diabetes, peripheral vascular disease, etc. are also eligible for reimbursement under the current coverage policy, provided the primary indication for treatment with EECP® therapy is angina or angina equivalent symptoms and the patient satisfies other listed criteria. Additionally, we have engaged

a consulting firm in a two-year agreement to assist us in extending CMS coverage and reimbursement to NYHA Class II/III heart failure. Please see the “Reimbursement” section of this Form 10-K for a more detailed discussion of reimbursement issues.

Other Potential Applications of EECP® Therapy

While currently we only have FDA clearance to market EECP® therapy in the United States for the treatment of stable and unstable angina, congestive heart failure, acute myocardial infarction and cardiogenic shock, there are many clinical papers published in peer reviewed medical journals demonstrating the safety and effectiveness in off-label applications by physicians, both domestic and overseas. During the past several years, many studies have been carried out to provide scientific evidence-based explanation on the mechanisms of action of EECP® therapy. Results of these studies show that EECP® therapy improves endothelial function in dilating vasculature, stimulates angiogenesis in forming new blood vessels, reduces inflammatory responses in deactivating signaling proteins and attenuates the atherosclerotic process by limiting smooth muscle cells proliferation and migration. These actions, demonstrated in scientific studies and published in peer reviewed medical society journals, have led physicians to use EECP® therapy in the treatment of many different cardiovascular symptoms, such as:

- Cerebral vascular disease, specifically ischemic stroke.
- Cardiac syndrome X
- Erectile dysfunction
- Chronic kidney disease
- Diabetes mellitus

It is believed that there is sufficient clinical and scientific evidence in these and other potential applications to demonstrate EECP® therapy's safety and efficacy. However, large randomized control studies appear to be needed to confirm the preliminary findings and drive market clearance and reimbursement.

We will continue to observe development in the use of EECP® therapy in new applications and may continue to sponsor clinical studies seeking regulatory clearance and reimbursement as funding becomes available.

The EECP® Therapy Systems

The EECP® therapy systems are noninvasive treatment systems utilizing fundamental hemodynamic principles to augment coronary blood flow and, at the same time, reduce the workload of the heart while improving the overall vascular function. The treatment is completely noninvasive and is administered to patients on an outpatient basis, usually in daily one-hour sessions, five days per week over seven weeks for a total of 35 treatments. The procedure is well tolerated and most patients begin to experience relief of chest pain caused by their coronary artery disease after 15 to 20 hours of therapy. As demonstrated in the clinical studies on EECP® therapy, positive effects have been shown in most patients to continue for years following a full course of therapy.

Clinical Studies on EECP® Therapy

There are at least 160 papers published in peer-reviewed medical journals related to EECP® therapy since 1992, and many more published in scientific and medical conferences all over the world. Most of these journal publications are clinical reports on the results in patients with chronic stable angina and/or heart failure. With only a few exceptions, these reports are generated using Vasomedical EECP® therapy systems. In summary, this body of literature contains evidence from a variety of institutions and investigators demonstrating the pathophysiological mechanisms underlying the benefits of EECP® therapy and the beneficial clinical outcomes of EECP® therapy, as follows:

Mechanisms of Action

In the past several years, the mechanisms of action of EECP® therapy have been the subjects of many investigations. It is now clear that during EECP® therapy the hemodynamic effect increases the pressure gradient across coronary

stenosis, induces higher shear stress on the endothelial monolayer, promotes angiogenesis and collateral development, improves endothelial functions, and reduces circulating proinflammatory cytokines, arterial stiffness and smooth muscle cells proliferation and migration, slowing down the progression of atherosclerotic processes. EECP® therapy:

- produces significant increase in coronary blood flow, cardiac output, left ventricular unloading documented by intracoronary pressure ultrasound Doppler study;
- stimulates development of angiogenesis and arteriogenesis resulting in recruitment of collateral circulation documented by intracoronary pressure wire measurements;
- improves endothelial function by increased plasmas nitric oxide and decreased endothelin-1 levels, producing vasodilation;
- neutralizes reactive oxygen species by reduction of 8-isoprostane and asymmetrical dimethylarginine, reducing cells injury;
- reduces inflammatory cytokines including tumor necrosis factor- α , monocyte chemoattractant protein-1, soluble vascular cell adhesion molecule and high-sensitivity C-reactive protein;
- increases release of endothelial progenitor cell, improves endothelial functions and reduces smooth muscle cells migration and proliferation;
- increases release of neurohormonal factors including angiotensin-II, ANP, BNP, improving control of vascular tone;
 - reduces arterial stiffness, reducing blood pressure and resistance to blood flow; and
 - increases flow-mediated dilation of the brachial and femoral arteries.

Beneficial Clinical Outcomes of EECP® Therapy

- increases myocardial perfusion to ischemic regions of the heart in patients with coronary artery disease (CAD), documented by radionuclide stress tests, improving cardiac functions;
 - eliminates or reduces angina and heart failure symptoms;
 - improves exercise capacity in patients with CAD;
- improves angina function class determined by Canadian Cardiovascular Society, improving functional capacity in patients with CAD and heart failure;
 - reduces frequency of angina episodes and nitroglycerin usage in patients with refractory angina;
 - improves quality of life in patients with angina and heart failure;
 - eliminates or reduces the use of anti-angina medications;
 - Benefits are sustained for up to three to five years.

Independent research aiming to fully explain the precise scientific means by which EECP® therapy achieves its long-term beneficial effects continues to be conducted and published every year. There is evidence to suggest that the EECP® therapy triggers a neurohormonal response that induces the production of growth and vasodilatation factors that promotes recruitment of new arteries and dilates existing blood vessels. The recruitment of new arteries, known as collateral blood vessels, bypass blocked or narrowed vessels and increase blood flow to ischemic areas of the heart muscle that were receiving an inadequate supply of blood. There is also evidence to support a mechanism related to improved function of the endothelium (the inner lining of the blood vessels), which regulates the luminal size of the arteries and controls the dilation of the arteries to ensure adequate blood flow to all organs, thus reducing constriction of blood vessels that supply oxygenated blood to the body's organs and tissues and as a result the reduced workload of the heart.

Significant Economic Benefits of EECP® Therapy

Beginning in 1998, we sponsored the International EECP® Patient Registry (IEPR™) with the Department of Epidemiology Data Center at the University of Pittsburgh, Graduate School of Public Health as the coordinating center responsible for data collection, processing, as well as performing error and consistency checks and analysis. The IEPR™ is a voluntary registry recording consecutive patients enrolled in clinical sites undergoing for at least 1 hour of EECP® therapy. There are at least 26 papers published in medical peer-reviewed journals and more

than 85 presentations in major scientific/clinical conferences using data collected in the IEPR™. The IEPR™ also examined the economic impact of EECP® treatment by collecting data on emergency department (ED) visits and hospitalizations in patients with refractory angina and LVD. Patients with refractory angina and LVD exert an enormous burden on health care resources primarily because of the number of recurrent emergency department (ED) visits and hospitalizations. Results from 450 patients with LVD (ejection fraction no more than 40%) treated with EECP® therapy for their refractory angina with data on all-cause ED visits and hospitalization rates within six months before EECP® therapy were compared with those at six months after EECP® therapy, and were analyzed and published in Congestive Heart Failure in February 2007. Despite the unfavorable risk profile, refractory angina patients with LVD achieved a substantial reduction in all-cause ED visits and hospitalization rates at 6-month follow-up. The mean number of ED visits per patient decreased from 0.9 ± 2.0 pre-EECP to 0.2 ± 0.7 at 6 months, and hospitalizations were reduced from 1.1 ± 1.7 to 0.3 ± 0.9 . The significant reduction in ED visits and hospitalizations post-EECP® therapy is consistent with findings presented elsewhere. EECP® therapy has the potential to save billions in healthcare costs each year, and the Company is educating payers on these benefits as part of its campaign to expand reimbursement.

Registry data, while considered a valuable source of complementary clinical data, is deemed by researchers and others to be less convincing than data from randomized and blinded clinical trials and from certain other well-controlled clinical study designs. There can be no assurance that the Company will be able to obtain regulatory, reimbursement or other types of approvals, or a favorable standing in medical professional practice guidelines, based only upon results observed in patients enrolled in registries.

Sales and Marketing – EECP®

Domestic Operations

We sell EECP® therapy systems, ambulatory monitoring devices and patient management devices to treatment providers such as hospitals, clinics and physician private practices in the United States through a combination of employees and independent sales representatives managed by a vice president of sales and marketing, along with in-house administrative support. The efforts of our sales organization are further supported by clinical educators who are responsible for the onsite training of physicians and therapists as new centers are established. This clinical applications group also engages in training and certification of new personnel at each site, as well as in updating providers on new clinical developments relating to EECP® therapy. The Company also markets certain products, accessories and supplies through an online store.

Our marketing activities support physician education and physician outreach programs, exhibition at national, international and regional medical conferences, as well as sponsorship of seminars at professional association meetings. These programs are designed to support our field sales organization and increase awareness of EECP® therapy in the medical community. Our marketing activities also include promotion of awareness among third-party payers and potential patients of the benefits of EECP® treatment for patients suffering from CHF as well as angina. In 2011, we also retained the services of a public relations group to assist us in promoting awareness for potential future growth as well as to support our current medical providers.

We employ service technicians for the repair and maintenance of EECP® systems and, in some instances, on-site training of a customer's biomedical engineering personnel. We provide a service arrangement at the time of equipment sale that includes: service by factory-trained service representatives, material and labor costs, emergency and remedial visits, software upgrades, technical phone support and preferred response times. After the service arrangement expires, we service our customers after the service arrangement expires either under separately purchased annual service contracts or on a fee-for-service basis.

International Operations

We distribute our EECP® products in the international market primarily through a network of independent distributors. It has generally been our policy to appoint distributors with exclusive marketing rights to EECP® therapy systems in their respective countries or regions, in exchange for their commitment to meet the duties and responsibilities required of a distributor. Each distribution agreement contains a number of requirements that must be met for the distributor to retain exclusivity, including minimum performance standards. Duties of the distributors include registering the product and obtaining necessary regulatory or clinical approvals to support local registration or reimbursement for EECP® therapy, as well as clinical and technical support to the therapy providers in their respective territories.

Our international marketing activities include, among other things, assisting distributors in obtaining regulatory clearance and national or third-party healthcare insurance reimbursement approval, participating in trade shows and medical conferences to create greater awareness and acceptance of EECP® therapy by clinicians, and identifying additional distribution channels in those countries in which we do not currently have a presence.

International sales may be subject to certain risks, including export/import licenses, tariffs, and other trade regulations. In addition, there can be no assurance that we will be successful in maintaining our existing distribution agreements or entering into any additional distribution agreements, or that our international distributors will be successful in marketing EECP® therapy.

Competition in the EECP® Market

While we believe that we are the industry leader, we are aware of at least three direct competitors with an external counterpulsation device on the U.S. market and two additional competitors in the international market. Some other companies have also received FDA 510(k) clearance for external counterpulsation systems since 1998, although we have not seen these systems commercially available in the marketplace. While we believe that these competitors' involvement in the market is limited, there can be no assurance that these companies will not become a significant competitive factor or that other companies will not enter the external counterpulsation market.

We view other companies engaged in the development of device-related, biotechnological or pharmacological approaches to the management of cardiovascular disease as potential competitors in the marketplace as well. These include such common and well-established medical devices and treatments as the intra-aortic balloon pump (IABP), ventricular assist devices (VAD), coronary artery bypass graft surgery (CABG), coronary angioplasty, mechanical circulatory support (MCS), transmyocardial laser revascularization (TMR), total artificial hearts, cardiac resynchronization devices, spinal cord stimulation (SCS), ranolazine and nesiritide (Natrecor®); as well as newer technologies such as gene therapy.

Government Regulations on EECP® Systems

We are subject to extensive regulation by numerous government regulatory agencies, including the FDA and similar foreign agencies. We are required to comply with applicable laws, regulations and standards governing the development, preclinical and clinical testing, manufacturing, quality testing, labeling, promotion, import, export, and distribution of our medical devices.

Clearance by U.S. FDA

Our EECP® therapy systems are currently classified by the US FDA as Class III devices, which include devices for which there is insufficient information demonstrating that general and special controls will provide reasonable assurance of safety and effectiveness, and which are life-sustaining, life-supporting or implantable devices, are of substantial importance in preventing impairment of human health, or pose a potential unreasonable risk of illness or injury. The FDA generally must clear a Class III device for marketing in the United States by a premarket approval (PMA), unless it is considered as a preamendments device – device that was commercially distributed before May 28, 1976 – and thus can be cleared by premarket notification, or 510(k). The Company's initial system received FDA 510(k) clearance in 1995, with later models receiving clearance at various times between 2000 and 2004.

Modifications to a previously cleared medical device that do not significantly affect its safety and effectiveness or constitute a major change in the intended use can be made without having to submit a new 510(k). Vasomedical followed relevant FDA guidance and concluded that the changes incorporated into its Model TS4 did not require a new 510(k) prior to its introduction to market. Vasomedical subsequently obtained a 510(k) that applied to the Model TS4 and all of its models in March 2004, when it made changes to the labeling of all of its EECP® therapy systems. In November 2004, Model Lumenair and AngioNew®-VI were introduced, and again it was concluded that the changes did not require a new 510(k).

There can be no assurance that all the necessary FDA clearances or approvals, including approval of any PMA required by the promulgation of a regulation, will be granted for our products, future-generation upgrades or newly

developed products, on a timely basis or at all. Failure to receive, or delays in receipt of such clearances, could have a material adverse effect on our financial condition and results of operations.

Clinical Trials

If human clinical trials of a device are required, whether to support a 510(k) or PMA application, the trials' sponsor, which is usually the manufacturer of the device, first must obtain the approval of the appropriate institutional review boards. If a trial is of a significant risk device, the sponsor also must obtain an investigational device exemption, or IDE, from the FDA before the trial may begin. For all clinical testing, the sponsor must obtain informed consent from the patients participating in each trial. There is no guarantee that the sponsor, whether Vasomedical or others, will obtain all necessary approvals, exemptions and consents before future clinical trials, and furthermore, the results of clinical testing that a sponsor undertakes may be insufficient to obtain clearance or approval of the tested product.

Pervasive and Continuing FDA Regulation

We are also subject to other FDA regulations that apply prior to and after a product is commercially released. These include the current Good Manufacturing Practice (cGMP) requirements, set forth in FDA's Quality System Regulation (QSR), that require manufacturers to have a quality system for the design, manufacture, packaging, labeling, storage, installation and servicing of medical devices intended for commercial distribution in the United States. This regulation covers various areas including management and organization, device design, purchase and handling of components, production and process controls such as those related to buildings and equipment, packaging and labeling control, distribution, installation, complaint handling, corrective and preventive action, servicing, and records. We are subject to periodic and random inspections by the FDA for compliance with the cGMP requirements and Quality System Regulation.

The FDA also enforces post-marketing controls that include the requirement to submit medical device reports to the agency when a manufacturer becomes aware of information suggesting that any adverse events are related to its marketed products. The FDA relies on medical device reports to identify product problems and utilizes these reports to determine, among other things, whether it should exercise its enforcement powers. The FDA also may require post-market surveillance studies for specified devices.

We are subject to the Federal Food, Drug, and Cosmetic Act's, or FDCA's, general controls, including establishment registration, device listing, and labeling requirements. If we fail to comply with any requirements under the FDCA, we, including our officers and employees, could be subject to, among other things, fines, injunctions, civil penalties, and criminal prosecution. We also could be subject to recalls or product corrections, total or partial suspension of production, denial of premarket notification clearance or PMA approval, and rescission or withdrawal of clearances and approvals. Our products could be detained or seized, the FDA could order a recall, repair, replacement, or refund of our devices, and the agency could require us to notify health professionals and others that the devices present unreasonable risks of substantial harm to the public health.

The advertising of our products is subject to regulation by the Federal Trade Commission, or FTC. The FTC Act prohibits unfair or deceptive acts or practices in or affecting commerce. Violations of the FTC Act, such as failure to have substantiation for product claims, would subject us to a variety of enforcement actions, including compulsory process, cease and desist orders and injunctions, which can require, among other things, limits on advertising, corrective advertising, consumer redress and restitution, as well as substantial fines or other penalties.

As a sales channel partner, we are subject to various federal, state and local laws targeting fraud and abuse in the healthcare industry, including anti-kickback and false claims laws.

Foreign Regulation

In most countries to which we seek to export our EECPC® systems, a local regulatory clearance must be obtained. The regulatory review process varies from country to country and can be complex, costly, uncertain, and

time-consuming. Vasomedical EECP® systems are all manufactured in accordance with ISO 13485, the international standard for medical devices. All our current systems are CE marking certified for European Union countries, and covered by our Health Canada license.

We are also subject to audits by organizations authorized by foreign countries to determine compliance with laws, regulations and standards that apply to the commercialization of our products in those markets. Examples include auditing by a European Union Notified Body organization (authorized by a member state's Competent Authority) to determine conformity with the Medical Device Directives (MDD) and by an organization authorized by the Canadian government to determine conformity with the Canadian Medical Devices Regulations (CMDR).

There can be no assurance that we will obtain desired foreign authorizations to commercially distribute our products in those markets or that we will comply with all laws, regulations and standards that pertain to our products in those markets. Failure to receive or delays in receipt of such authorizations or determinations of conformity could have a material adverse effect on our financial condition and results of operations.

Patient Privacy

Federal and state laws protect the confidentiality of certain patient health information, including patient records, and restrict the use and disclosure of that protected information. The U.S. Department of Health and Human Services (HHS) published patient privacy rules under the Health Insurance Portability and Accountability Act of 1996 (HIPAA privacy rule) and the regulation was finalized in October 2002. Currently, the HIPAA privacy rule affects us only indirectly in that patient data that we access, collect and analyze may include protected health information. Additionally, we have signed some Business Associate Agreements with Covered Entities that contractually bind us to protect private health information, consistent with the HIPAA privacy rule's requirements. We do not expect the costs and impact of the HIPAA privacy rule to be material to our business.

Practice Guidelines for EECP® Therapy

Medical professional societies periodically issue Practice Guidelines to their members and make them available publicly. The American College of Cardiology (ACC) and the American Heart Association (AHA) have jointly engaged in developing practice guidelines since 1980 to critically evaluate the use of diagnostic procedures and therapies in the management or prevention of cardiovascular diseases. These guidelines are meant to "improve the effectiveness of care, optimize patient outcomes and affect the overall cost of care favorably by focusing resources on the most effective strategies." Recommendations incorporated into the guidelines are based upon an assessment of the strength of evidence for or against a treatment or procedure and estimates of expected health outcomes stemming from a formal review of peer-reviewed published literature. These guidelines may not be updated for some time.

The ACC/AHA 2002 Guideline Update for the Management of Patients with Chronic Stable Angina was issued in 2003. Comments on external counterpulsation appear in a section entitled Recommendations for Alternative Therapies for Chronic Stable Angina in Patients Refractory to Medical Therapy Who Are Not Candidates for Percutaneous Intervention or Surgical Revascularization and include a so-called Class IIb recommendation. ACC/AHA guideline classifications I, II and III are used to "provide final recommendations for both patient evaluation and therapy" and a Class IIb rating is defined as "Usefulness/efficacy is less well established by evidence/opinion."

An Update to the 2002 ACC/AHA Guidelines has been under review by the ACC Guidelines Committee for the Guideline Update for the Management of Patients with Chronic Stable Angina and was originally scheduled for release in spring 2011. Based upon the publication of numerous randomized, controlled studies in the last several years on the mechanisms of action of EECP® therapy, the Company made a formal request, and has contacted all domestic EECP® providers and key opinion leaders in the field of cardiology to support its request, for an upgrade from the Class IIb classification to a IIa level, consistent with the current published scientific evidence. The update has been delayed; however, we have been advised by the ACC that a new release date has been scheduled for mid-summer 2012.

The ACC/AHA 2005 Guidelines for the Diagnosis and Management of Chronic Heart Failure in the Adult was issued in 2005. External counterpulsation is listed as one of the devices under investigation in a section entitled "Drugs and Interventions Under Active Investigation." The 2006 Comprehensive Heart Failure Practice Guideline, issued in February 2006 by the Heart Failure Society of America, does not include any comments on the use of external counterpulsation therapy for treating heart failure patients.

In summary, while there is still some reluctance in the cardiology community about the broader use of EECP® therapy, positive evaluations of its application for patients with chronic angina and heart failure continue to appear in presentations at major scientific meetings and in peer-reviewed publications each year. We believe the new evidence from completed and ongoing studies regarding the efficacy of EECP® therapy and its long lasting effect will be sufficient to warrant a modification of practice guidelines to a more favorable recommendation, increased acceptance by the medical community, and broader reimbursement coverage.

Reimbursement for EECP® Therapy

Reimbursement coverage and payment rates are important factors in the sales of our products, and we depend in large part on the availability of reimbursement programs. Medicare, Medicaid, as well as private health care insurance and managed-care plans determine eligibility for coverage of a product or therapy based on a number of factors, including the payer's determination that the product is reasonable and necessary for the diagnosis or treatment of the illness or injury for which it is administered according to the scope of clinical evidence available, accepted standards of medical care in practice, the product's cost effectiveness, whether the product is experimental or investigational, impact on health outcomes and whether the product is not otherwise excluded from coverage by law or regulation.

Our reimbursement strategies are currently focused in the following areas: expanding coverage to include heart failure and mild angina, modifying reimbursement policy language to allow for EECP® therapy as a first line treatment for severe angina, increasing the reimbursement rate of current coverage, and obtaining coverage in selected international markets.

Current Medicare Coverage in Angina

In February 1999, CMS, the federal agency that administers the Medicare program for approximately 47.7 million beneficiaries now, issued a national coverage policy under HCPCS code G0166 for the use of the EECP® therapy system. Key excerpts from the coverage read as follows:

“Although ECP devices are cleared by the Food and Drug Administration (FDA) for use in treating a variety of cardiac conditions, including stable or unstable angina pectoris, acute myocardial infarction and cardiogenic shock, the use of this device to treat cardiac conditions other than stable angina pectoris is not covered, since only that use has developed sufficient evidence to demonstrate its medical effectiveness.”

“... for patients who have been diagnosed with disabling angina (class III or class IV, Canadian Cardiovascular Society Classification or equivalent classification) who, in the opinion of a cardiologist or cardiothoracic surgeon, are not readily amenable to surgical interventions such as balloon angioplasty and cardiac bypass because:

1. their condition is inoperable, or at high risk of operative complications or post-operative failure;
2. their coronary anatomy is not readily amenable to such procedures; or
3. they have co-morbid disease states, which create excessive risk.”

The physician office setting and the hospital outpatient facility are the only entities currently authorized to receive reimbursement for the EECP® therapy under the Medicare program and reimbursement is not permitted to other individuals or entity types, which include, but are not limited to, nurse practitioners, physical therapists, ambulatory surgery centers, nursing homes, comprehensive outpatient rehabilitation facilities, outpatient dialysis facilities, and independent diagnostic testing facilities. The 2012 national average payment rate per hourly EECP® therapy session in the physician office setting and the hospital outpatient facility is \$151 and \$94, respectively. Actual reimbursement rates vary throughout the country and range from \$126 to \$204 per hourly EECP® therapy session in the physician office setting. The national average payment rate varied considerably (from \$130 in 2000 to \$208 in 2003 for physician offices), but has become stable since 2004, as in the summary below:

| Year | Physician Office | Hospital |
|------|------------------|----------|
| 2004 | \$137 | \$113 |
| 2005 | \$138 | \$102 |
| 2006 | \$138 | \$104 |
| 2007 | \$147 | \$107 |
| 2008 | \$156 | \$109 |
| 2009 | \$150 | \$102 |
| 2010 | \$148 | \$104 |
| 2011 | \$153 | \$102 |
| 2012 | \$151 | \$94 |

If there were any material change in the availability of Medicare coverage, or if the reimbursement level for treatment procedures using the EEC[®] therapy system is determined to be inadequate, it would adversely affect our business, financial condition and results of operations. Moreover, we are unable to forecast what additional legislation or regulation, if any, relating to the health care industry or Medicare coverage and payment level may be enacted in the future, or what effect such legislation or regulation would have on our business.

Application to Expand Medicare Coverage to include Class II Angina and Class II/III CHF

On May 31, 2005, we submitted to CMS, and on June 20, 2005, CMS accepted our application for expansion of reimbursement coverage of EEC[®] therapy to include patients with NYHA Class II/III stable heart failure symptoms with an ejection fraction of less than or equal to 35%, i.e. chronic, stable, mild-to-moderate systolic heart failure as a primary indication, as well as patients with CCSC II, i.e. chronic, stable mild angina.

On March 20, 2006, CMS issued their Decision Memorandum regarding the applications with the opinion “that the evidence is not adequate to conclude that external counterpulsation therapy is reasonable and necessary for the treatment of” the additional indications as requested. They did, however, reiterate in the Decision Memorandum that “Current coverage as described in Section 20.20 of the Medicare National Coverage Determination (NCD) manual will remain in effect” for refractory angina patients. We had subsequently submitted to CMS more data and publications from our PEECH[™] study and were advised to continue to gather more clinical evidence for future submission.

Based on the new clinical evidence in the past five years, we have started an initiative campaigning for a positive medical necessity decision in support of the use of EEC[®] therapy in the treatment of heart failure. At the same time, we will continue to educate the marketplace that EEC[®] therapy is a therapy for ischemic cardiovascular disease and that patients with a primary diagnosis of heart failure, diabetes, peripheral vascular disease, etc., are also eligible for reimbursement under the current coverage policy, provided the primary indication for treatment with EEC[®] therapy is angina or angina equivalent symptoms and the patient satisfies other listed criteria.

Coverage with Other Third-Party Payers

Since the establishment of reimbursement for EEC[®] therapy by the federal government, an increasing number of private third-party payers have routinely provided coverage for the use of EEC[®] therapy for the treatment of angina and have issued positive coverage policies, which are generally similar to Medicare’s coverage policy in scope. In addition, some third-party payers began limited coverage of EEC[®] therapy for the treatment of CHF. On the other hand, there are private insurance carriers that continue to adjudicate EEC[®] treatment claims on a case-by-case basis.

We continue to pursue a constructive dialogue with many private insurers for the establishment of positive and expanded coverage policies for EEC[®] treatment that include CHF patients and have engaged a consulting firm to

assist us in co-sponsoring a study with a major commercial healthcare third-party payer demonstrating the efficacy, efficiency, and/or cost effectiveness of EECP® therapy for NYHA Class II/III heart failure.

If there were any significant reduction in the availability of third-party private insurers or the adequacy of the reimbursement level for treatment procedures using the EECP® therapy system, it would adversely affect our business, financial condition and results of operations. Moreover, we are unable to forecast what additional legislation or regulation, if any, relating to the health care industry or third-party private insurers' coverage and payment levels may be enacted in the future or what effect such legislation or regulation would have on us.

Reimbursement in International Markets

The reimbursement environment for EEC[®] therapy in international markets is fragmented and coverage varies. Our reimbursement strategy has changed to be more proactive and create opportunities through our distribution partners. Our current efforts on behalf of EEC[®] therapy in both the private and public healthcare sectors of selected international markets are being initiated jointly by the company and its distributors in their designated territories. We do not anticipate a significant impact on financial performance in the next fiscal year, given the long lead time from submission to approval of international dossiers for each reimbursement authority.

Other Medical Equipment

In our effort to diversify our medical equipment offering, in May 2008 we first obtained exclusive distribution rights for the BIOX[™] series ECG Holter and ambulatory blood pressure monitoring products in the North American market. Between April 2009 and June 2011 the Company received multiple 510(k) clearances from the US FDA for various BIOX series ECG Holter, ambulatory blood pressure and combination monitors. The Company now offers a complete line of BIOX[™] series diagnostic products for ambulatory monitoring needs.

In September 2011, the Company acquired BIOX and now includes its operations in its consolidated financial results. In combination with BIOX, the Company is also promoting its joint R&D and manufacturing capabilities to secure OEM opportunities in the United States as well as pursuing international sales opportunities for the product line through its global distribution channel.

The growing market for ECG Holter and ambulatory blood pressure monitoring products worldwide is expected to exceed \$150 million by 2015. While there are multiple competitors in the marketplace, we believe that due to certain special features of our products, and through our sales and marketing efforts in niche markets, we will increase sales revenue and create opportunities for other products the Company manufactures or distributes.

The BIOX[™] series ECG Holter and ambulatory blood pressure monitoring products are manufactured by Biox Instruments Co. Ltd. (BIOX) in Wuxi, China, under the current Good Manufacturing Practice (cGMP) requirements as set forth in the FDA Quality System Regulation as well as ISO 13485 standard, the international quality standard for medical device manufacturers. Biox's manufacturing facility has also been certified to conform to full quality assurance system requirements of the EU Medical Device Directive and other requirements by various government authorities. These medical products have been classified by the U.S. FDA as Class II products.

Additionally, the Company continues to distribute a line of private label patient management products first introduced in April 2009. These products include the hand held EZ ECG[™] Monitor, the EZ O2[™] Adult and EZ O2[™] Pediatric Pulse Oximeters, and the EZ O2[™] Wrist Oximeter.

Strategic Objectives

Our short- and long-term plans for the growth of the Company and its stockholder value are:

- a) Maintain and grow our equipment business, by
 - i) Continuing to align the cost structure with revenue growth, including increased funding of marketing initiatives;
 - ii) Expanding our direct sales force to significantly increase revenue, particularly from EEC[®] equipment and service sales; and
 - iii) Increasing our international efforts to grow international sales of all our device offerings; and
 - iv) Pursuing accretive acquisitions of medical device companies in the international marketplace.
- b) Continue to diversify our product offerings, by

- i) Identifying and introducing other medical device products and opportunities that fit into our target market; and
 - ii) Working with select partners to develop our medical device OEM business.
 - c) Work with consultants to expand reimbursement coverage for EECP® therapy, by
- i) Submitting up-to-date treatment effectiveness data and cost saving evidence to CMS and third party payers for consideration of EECP® as a first line treatment option for angina and for expansion of coverage to include heart failure; and
- ii) Possibly conducting clinical trials to expand coverage, including the potential use of EECP® as a treatment for other ailments including diabetes, chronic kidney disease, and erectile dysfunction.
- d) Maintain and improve business performance in our sales representation segment by expanding the GE Healthcare product modalities we represent, and possibly building new teams to represent other vendors.

The above-listed strategic objectives are forward-looking statements. We review, modify and change our strategic objectives from time to time based upon changing business conditions. There can be no assurance that we will be able to achieve our strategic objectives and, even if these results are achieved, risks and uncertainties could cause actual results to differ materially from anticipated results. Financial resource availability may reduce our ability to achieve these strategic objectives. Please see the section of this Form 10-K entitled “Risk Factors” for a description of certain risks, among others that may cause our actual results to vary from the forward-looking statements.

Intellectual Properties

We own eleven US patents including eight utility patents and three design patents that expire at various times between now and 2023. We will from time to time file other patent applications regarding specific enhancements to the current EECP® models, future generation products, and methods of treatment in the future. Moreover, trademarks have been registered for the names “EECP”, “AngioNew”, “Natural Bypass”, “Vasomedical”, “Vasomedical EECP” and “VasoHealthcar

Through our China-based subsidiaries, we own three utility patents and various trademarks. We also own five software copyright certificates in China, related to Holter ECG and ambulatory blood pressure data analysis. We pursue a policy of seeking patent protection, both in the US and abroad, for our proprietary technology. We believe that we have a solid patent foundation in the field of external counterpulsation devices and that the number of patents and applications demonstrates our technical leadership, dating back to the mid-1980s. Our patent portfolio focuses on the areas of external counterpulsation control and the overall design and arrangement of the external counterpulsation apparatus, including the console, treatment bed, fluid distribution, and inflatable cuffs. None of our current competitors have a significant patent portfolio in the area of external counterpulsation devices.

There can be no assurance that our patents will not be violated or that any issued patents will provide protection that has commercial significance. As with any patented technology, litigation could be necessary to protect our patent position. Such litigation can be costly and time-consuming, and there can be no assurance that we will be successful. The loss or violation of our EECP® patents and trademarks could have a material adverse effect upon our business.

Employees

As of December 31, 2011, we employed approximately 175 full-time persons, of which 28 are employed through our facility in Westbury, New York, 82 through our VasoHealthcare subsidiary and 65 are in China. None of our employees are represented by a labor union. We believe that our employee relations are good.

The Company also uses several part-time employees and consultants from time to time for various purposes.

Manufacturing

Vasomedical Solutions maintains its manufacturing facility in the Westbury, NY location to satisfy domestic and international needs for the TS4 and Lumenair EEC[®] systems, and Vasomedical Global operates production facilities at the Life Enhancement Technology Co. Ltd. (LET) and BIOX facilities in China. LET manufactures AngioNew[®] and Lumenair EEC[®] systems and Biox manufactures ambulatory monitoring devices. Our VasoHealthcare subsidiary maintains an office in Greensboro, North Carolina.

All manufacturing operations are conducted under the current Good Manufacturing Practice (cGMP) requirements as set forth in the FDA Quality System Regulation as well as ISO 13485 standard, the international quality standard for medical device manufacturers. We are also certified to conform to full quality assurance system requirements of the EU Medical Device Directive and can apply CE marking to all of our current product models. Lastly, we are certified to comply with the requirements of the Canadian Medical Device Regulations (CMDR) and, for all our EEC[®] systems, with all UL safety requirements. All these regulations and standards subject us to inspections to verify compliance and require us to maintain documentation and controls for the manufacturing and quality activities.

We believe our manufacturing capacity and warehouse facility are adequate to meet the current and immediately foreseeable future demand for the production of our medical devices. We believe our suppliers of the other medical devices we distribute or represent are capable of meeting our demand for the foreseeable future.

Recent Development

We have scheduled a meeting with GEHC to discuss the recent resignations of three members of management of our Vaso Healthcare subsidiary, including its Chief Operating Officer. The COO resigned effective immediately and the other two members of management resigned effective mid-May 2012. While the Company is in the process of filling these positions, and has engaged on an interim basis a consultant to supervise the business operations, we will be discussing with GEHC, among other things, the impact of these resignations on the GEHC relationship. The agreement with GEHC remains in full force and effect.

ITEM 1A - RISK FACTORS

Investing in our common stock involves risk. You should carefully consider the following information about these risks together with the other information contained in this Annual Report on Form 10-K. If any of the following risks actually occur, our business could be harmed. This could cause the price of our stock to decline, and you may lose part or all of your investment.

Financial Risks

The sustainability of the profit achieved in the current period is dependent on several factors.

Our ability to sustain the profitability achieved in the current period is dependent on many factors, primarily being the sufficient and timely generation and recognition of revenue in our Sales Representation segment, the success of our marketing and sales efforts in the Equipment segment, as well as the success of our other strategic initiatives, including our China acquisitions.

Risks Related to Our Business

We currently derive a significant amount of our revenue from our agreement with GEHC and currently our continued growth is dependent on this agreement.

On May 19, 2010, we signed a sales representation agreement with GEHC, the healthcare business unit of the General Electric Company, for the sale of select GEHC diagnostic imaging products. Under the GEHC Agreement, we have been appointed the exclusive representative for these products to specific market segments in the 48 contiguous states of the United States and the District of Columbia. The GEHC Agreement has an initial term of three years commencing July 1, 2010, subject to extension and also subject to earlier termination under certain circumstances.

The significant amount of our current period and fiscal 2011 revenue and net income arose from activities under this contract. Moreover, our growth depends partially on the territories assigned to VasoHealthcare by GEHC, and thus relies on our ability to demonstrate our added value as a channel partner, and maintain a positive relationship with GEHC. There is no assurance that the agreement will be renewed before it expires or terminated prior to its expiration pursuant to its termination provisions. Should GEHC terminate or not renew the agreement, it would have a material adverse effect on our financial condition and results of operations. See also Recent Development above.

We are materially dependent on the expansion of medical reimbursement for treatment procedures using EECP® therapy in order to achieve significant growth in the domestic EECP® market.

The growth of our domestic EECP® business is dependent on current medical reimbursement policies, which provide coverage for a restricted class of heart patients. While we continue our dialogue with CMS and commercial payers to obtain expanded coverage for EECP® therapy, there is no assurance that the Company will succeed in such efforts.

If we do not receive expanded medical coverage for the use of EECP® therapy, it will adversely affect our domestic EECP® therapy business.

Material changes in the availability of Medicare, Medicaid or third-party reimbursement at adequate price levels could adversely affect our domestic EECP® business.

Health care providers, such as hospitals and physician private practices in the U.S., that purchase or lease medical devices such as the EECP® therapy system for use on their patients generally rely on third-party payers, principally Medicare, Medicaid and private health insurance plans, to reimburse all or part of the costs and fees associated with the procedures performed with these devices. If there were any significant reduction in the availability of Medicare, Medicaid or other third-party coverage or the adequacy of the reimbursement level for treatment procedures using the EECP® therapy system, it would adversely affect our domestic EECP® business, financial condition and results of operations. Moreover, we are unable to forecast what additional legislation or regulation, if any, relating to the health care industry or Medicare or Medicaid coverage and payment level may be enacted in the future or what effect such legislation or regulation would have on our business. Even if a device has FDA clearance, Medicare, Medicaid and other third-party payers may deny reimbursement if they conclude that the device is not “reasonable and necessary” according to their criteria. In addition, reimbursement may not be at, or remain at, price levels adequate to allow medical professionals and hospitals in the U.S. to realize an appropriate return on the purchase of our products.

Increased acceptance of EECP® therapy by the medical community is important for the growth of our EECP® business.

While positive evaluations of the application of EECP® therapy continue to appear in presentations at major scientific meetings and in peer-reviewed publications each year, there is still skepticism concerning EECP® therapy methodology. The American Heart Association and the American College of Cardiology Practice Guidelines currently list EECP® as a therapy currently under investigation for treatment of heart failure and have a classification rating of IIb as a treatment for angina patients who are refractory to medical therapy and are not candidates for percutaneous coronary intervention (PCI) or coronary artery bypass grafting (CABG). A classification rating of IIb indicates the usefulness/efficacy of EECP® therapy is less well established by evidence/opinion. The medical community utilizes these guidelines when considering the various treatment options for their patients. Certain cardiologists, in cases where the EECP® therapy is a viable alternative, still appear to prefer percutaneous coronary interventions (e.g. balloon angioplasty and stenting) and cardiac bypass surgery for their patients. Additional evidence regarding the efficacy of EECP® therapy continues to evolve, however the evidence may not be sufficient to warrant a modification of these guidelines to a more favorable recommendation and increased acceptance by the medical community. We are dependent on consistency of favorable research findings about EECP® therapy and increasing acceptance of EECP® therapy as a safe, effective and cost effective alternative to other available products by the medical community for growth.

We face competition from other companies and technologies.

We compete with other companies that market medical devices in the global medical device marketplace. We do not know whether these companies, or other potential competitors who may be developing medical devices, may succeed in developing technologies or products that are more efficient than those offered by us, and that would render our

technology and existing products obsolete or non-competitive. Potential new competitors may also have substantially greater financial, manufacturing and marketing resources than those possessed by us. In addition, other technologies or products may be developed that have an entirely different approach or means of accomplishing the intended purpose of our products. Accordingly, the life cycles of our products are difficult to estimate. To compete successfully, we must keep pace with technological advancements, respond to evolving consumer requirements and achieve market acceptance.

We may not continue to receive necessary FDA clearances or approvals, which could hinder our ability to market and sell our products.

If we modify our medical devices and the modifications significantly affect safety or effectiveness, or if we make a change to the intended use, we will be required to submit a new premarket notification, or 510(k), to FDA. We would not be able to market the modified device in the U.S. until FDA issues a clearance for the 510(k).

Additionally, if FDA publishes a regulation requiring a premarket approval (PMA) application for the medical devices we market, we would then need to submit a PMA, and have it filed with the agency, by the date specified by FDA in its regulation. A PMA requires us to prove the safety and effectiveness of a device to the FDA. The process of obtaining PMA approval may require a clinical study and is expensive, time-consuming, and uncertain. If we did obtain PMA approval, any change after approval affecting the safety or effectiveness of the device will require approval of a PMA supplement.

If we offer new products that require 510(k) clearance or PMA approval, we will not be able to commercially distribute those products until we receive such clearance or approval. Regulatory agency approval or clearance for a product may not be received or may entail limitations on the device's indications for use that could limit the potential market for the product. Delays in receipt of, or failure to obtain or maintain, regulatory clearances and approvals, could delay or prevent our ability to market or distribute our products. Such delays could have a material adverse effect on our equipment business.

If we are unable to comply with applicable governmental regulations, we may not be able to continue certain of our operations.

We also must comply with current Good Manufacturing Practice (cGMP) requirements as set forth in the Quality System Regulation (QSR) to receive FDA approval to market new products and to continue to market current products. The QSR imposes certain procedural and documentation requirements on us with respect to manufacturing and quality assurance activities, including packaging, storage, and record keeping. Our products and activities are subject to extensive, ongoing regulation, including regulation of labeling and promotion activities and adverse event reporting. Also, our FDA registered facilities are subject to inspection by the FDA and other governmental authorities. Any failure to comply with regulatory requirements could delay or prevent our ability to market or distribute our products. Violation of FDA statutory or regulatory requirements could result in enforcement actions, such as voluntary or mandatory recalls, suspension or withdrawal of marketing clearances or approvals, seizures, injunctions, fines, civil penalties, and criminal prosecutions, all of which could have a material adverse effect on our business. Most states also have similar post-market regulatory and enforcement authority for devices.

Our operations in China are also subject to the laws of the People's Republic of China with which we must be in compliance in order to conduct these operations.

We are subject to various federal, state and local laws targeting fraud and abuse in the healthcare industry, including anti-kickback and false claims laws.

We cannot predict the nature of any future laws, regulations, interpretations, or applications, nor can we predict what effect additional governmental regulations or administrative orders, either domestically or internationally, when and if promulgated, would have on our business in the future. We may be slow to adapt, or we may never adapt to changes in existing requirements or adoption of new requirements or policies. We may incur significant costs to comply with laws and regulations in the future or compliance with laws or regulations may create an unsustainable burden on our business.

We may not receive approvals by foreign regulators that are necessary for international sales.

Sales of medical devices outside the United States are subject to foreign regulatory requirements that vary from country to country. Premarket approval or clearance in the United States does not ensure regulatory approval by other jurisdictions. If we, or any international distributors, fail to obtain or maintain required pre-market approvals or fail to comply with foreign regulations, foreign regulatory authorities may require us to file revised governmental notifications, cease commercial sales of our products in the applicable countries or otherwise cure the problem. Such enforcement action by regulatory authorities may be costly.

In order to sell our products within the European Union, we must comply with the European Union's Medical Device Directive. The CE marking on our products attests to this compliance. Future regulatory changes may limit our ability to use the CE mark, and any new products we develop may not qualify for the CE mark. If we lose this authorization or fail to obtain authorization on future products, we will not be able to sell our products in the European Union.

We depend on suppliers for the supply of certain products.

While we now manufacture our own EECP® product through one of our recent China acquisitions, we still depend on certain suppliers for parts, components and certain finished goods. While we do not foresee any difficulties in timely receiving products at competitive prices, the inability of not receiving products in timely fashion or at competitive prices would adversely affect our business. In addition, as a GEHC channel partner, we could be negatively impacted by interruptions or delays to equipment installations, production and quality issues, and other customer concerns related to GEHC.

We depend on management and other key personnel.

We are dependent on a limited number of key management and technical personnel. The loss of one or more of our key employees may harm our business if we are unable to identify other individuals to provide us with similar services. We do not maintain "key person" insurance on any of our employees. In addition, our success depends upon our ability to attract and retain additional highly qualified sales, management, manufacturing and research and development personnel in our various operations. We face competition in our recruiting activities and may not be able to attract or retain qualified personnel.

We may not have adequate intellectual property protection.

Our patents and proprietary technology may not be able to prevent competition by others. The validity and breadth of claims in medical technology patents involve complex legal and factual questions. Future patent applications may not be issued, the scope of any patent protection may not exclude competitors, and our patents may not provide competitive advantages to us. Our patents may be found to be invalid and other companies may claim rights in or ownership of the patents and other proprietary rights held or licensed by us. Also, our existing patents may not cover products that we develop in the future. Moreover, when our patents expire, the inventions will enter the public domain. There can be no assurance that our patents will not be violated or that any issued patents will provide protection that has commercial significance. Litigation may be necessary to protect our patent position. Such litigation may be costly and time-consuming, and there can be no assurance that we will be successful in such litigation.

The loss or violation of certain of our patents and trademarks could have a material adverse effect upon our business.

Since patent applications in the United States are maintained in secrecy until such patent applications are issued, our current product development may infringe patents that may be issued to others. If our products were found to infringe patents held by competitors, we may have to modify our products to avoid infringement, and it is possible that our modified products would not be commercially successful.

We do not intend to pay dividends in the foreseeable future.

We do not intend to pay any cash dividends on our common stock in the foreseeable future.

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Risks Related to Our Industry

Our growth could suffer if the markets into which we sell products decline, do not grow as anticipated or experience cyclicalities.

Our growth depends in part on the growth of the healthcare markets which we serve. Our quarterly sales and profits depend substantially on the volume and timing of orders installed during the fiscal quarter, and the installation of such orders is difficult to forecast. Product demand is dependent upon the customer's capital spending budget as well as government funding policies, and matters of public policy as well as product and economic cycles that can affect the spending decisions of these entities. These factors could adversely affect our growth, financial position, and results of operations.

Technological change is difficult to predict and to manage.

We face the challenges that are typically faced by companies in the medical device field. Our product line has required, and any future products will require, substantial development efforts and compliance with governmental clearance or approval requirements. We may encounter unforeseen technological or scientific problems that force abandonment or substantial change in the development of a specific product or process.

We are subject to product liability claims and product recalls that may not be covered by insurance.

The nature of our manufacturing operations exposes us to risks of product liability claims and product recalls. Medical devices as complex as ours frequently experience errors or failures, especially when first introduced or when new versions are released.

We currently maintain product liability insurance at \$5,000,000 per occurrence and \$6,000,000 in the aggregate. Our product liability insurance may not be adequate. In the future, insurance coverage may not be available on commercially reasonable terms, or at all. In addition, product liability claims or product recalls could damage our reputation even if we have adequate insurance coverage.

We do not know the effects of healthcare reform proposals.

The healthcare industry is undergoing fundamental changes resulting from political, economic and regulatory influences. In the United States, comprehensive programs have been suggested seeking to increase access to healthcare for the uninsured, control the escalation of healthcare expenditures within the economy and use healthcare reimbursement policies to balance the federal budget.

We expect that the United States Congress and state legislatures will continue to review and assess various healthcare reform proposals, and public debate of these issues will likely continue. There have been, and we expect that there will continue to be, a number of federal and state proposals to constrain expenditures for medical products and services, which may affect payments for products such as ours. We cannot predict which, if any of such reform proposals will be adopted and when they might be effective, or the effect these proposals may have on our business. Other countries also are considering health reform. Significant changes in healthcare systems could have a substantial impact on the manner in which we conduct our business and could require us to revise our strategies.

Risks Related to our Securities

The application of the "penny stock" rules could adversely affect the market price of our common stock and increase your transaction costs to sell those shares.

As long as the trading price of our common shares is below \$5 per share, the open-market trading of our common shares will be subject to the "penny stock" rules. The "penny stock" rules impose additional sales practice requirements on broker-dealers who sell securities to persons other than established customers and accredited investors (generally those with assets in excess of \$1,000,000 or annual income exceeding \$200,000 or \$300,000 together with their spouse). For transactions covered by these rules, the broker-dealer must make a special suitability determination for the purchase of securities and have received the purchaser's written consent to the transaction before the purchase. Additionally, for any transaction involving a penny stock, unless exempt, the broker-dealer must deliver, before the transaction, a disclosure schedule prescribed by the Securities and Exchange Commission relating to the penny stock market. The broker-dealer also must disclose the commissions payable to both the broker-dealer and the registered representative and current quotations for the securities. Finally, monthly statements must be sent disclosing recent price information on the limited market in penny stocks. These additional burdens imposed on broker-dealers may restrict the ability or decrease the willingness of broker-dealers to sell our common shares, and may result in decreased liquidity for our common shares and increased transaction costs for sales and purchases of our common shares as compared to other securities.

Our common stock is subject to price volatility.

The market price of our common stock historically has been and may continue to be highly volatile. Our stock price could be subject to wide fluctuations in response to various factors beyond our control, including, but not limited to:

- medical reimbursement;
- quarterly variations in operating results;
- announcements of technological innovations, new products or pricing by our competitors;
- the rate of adoption by physicians of our technology and products in targeted markets;
 - the timing of patent and regulatory approvals;
- the timing and extent of technological advancements;
 - results of clinical studies;
- the sales of our common stock by affiliates or other shareholders with large holdings; and
 - general market conditions.

Our future operating results may fall below the expectations of securities industry analysts or investors. Any such shortfall could result in a significant decline in the market price of our common stock. In addition, the stock market has experienced significant price and volume fluctuations that have affected the market price of the stock of many medical device companies and that often have been unrelated to the operating performance of such companies. These broad market fluctuations may directly influence the market price of our common stock.

Additional Information

We are subject to the reporting requirements under the Securities Exchange Act of 1934 and are required to file reports and information with the Securities and Exchange Commission (SEC), including reports on the following forms: annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and amendments to those reports files or furnished pursuant to Section 13(a) or 15(d) of the Securities Act of 1934.

ITEM 2 – PROPERTIES

We owned our 18,000 square foot headquarters and manufacturing facility at 180 Linden Avenue, Westbury, New York 11590, until August 15, 2007 when we sold it under a five-year leaseback agreement for \$1.4 million. The net proceeds from the sale was approximately \$425,000, after payment in full of the two secured notes on our facility, brokers fees, closing costs, and the opening of a certificate of deposit in accordance with the provisions of the new lease. The annual rental expense for the lease is approximately \$150,000. Our Westbury lease expires in August 2012 at which time we will either extend the lease or seek nearby facilities. We believe that our current facility is adequate for foreseeable current and future needs and that there will be no difficulty in acquiring comparable facilities if we do not extend our current lease.

We lease our engineering and production facilities in China. We lease approximately 9,000 square feet at an annual cost of approximately \$46,000 in Wuxi and approximately 11,000 square feet at an annual cost of approximately \$23,000 in Foshan.

Our Sales Representation segment primarily operates from a facility in Greensboro, North Carolina, where we lease 2,600 square feet of office space at an annual rental expense of approximately \$48,000.

PART II

ITEM 5 - MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

Our common stock currently trades on OTCQB, the middle tier of the OTC marketplace reserved for fully reporting issuers, under the symbol VASO.PK. On May 26, 2006, our common stock ceased trading on the NASDAQ Capital Market tier of the NASDAQ Stock Market and began trading on the NASD Pink Sheets. Effective June 20, 2006, our common stock began trading on the Over-the-Counter Bulletin Board (OTCBB). On February 22, 2011, our common stock was delisted from OTCBB and was quoted solely on OTC Link. The number of record holders of common stock as of April 23, 2012, was approximately 1,100, which does not include approximately 8,600 beneficial owners of shares held in the name of brokers or other nominees. The table below sets forth the range of high and low trade prices of the common stock for the fiscal periods specified.

| | June 1, 2011 - December 31, 2011 | | Fiscal 2011 | | Fiscal 2010 | |
|-----------------|-------------------------------------|---------|-------------|---------|-------------|---------|
| | High | Low | High | Low | High | Low |
| First quarter | \$ 0.51 | \$ 0.28 | \$ 0.24 | \$ 0.18 | \$ 0.09 | \$ 0.07 |
| Second quarter* | \$ 0.43 | \$ 0.21 | \$ 0.21 | \$ 0.18 | \$ 0.09 | \$ 0.06 |
| Third quarter | N/A | N/A | \$ 0.31 | \$ 0.18 | \$ 0.08 | \$ 0.05 |
| Fourth quarter | N/A | N/A | \$ 0.74 | \$ 0.34 | \$ 0.31 | \$ 0.05 |

* Second quarter is from September 1, 2011 through December 31, 2011 in the transitional period.

The last bid price of the Company's common stock on April 23, 2012, was \$0.26 per share.

Dividend Policy

We have never paid any cash dividends on our common stock and do not intend to pay cash dividends in the foreseeable future.

ITEM 7 - MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS.

This Management's Discussion and Analysis of Financial Condition and Results of Operations contains descriptions of our expectations regarding future trends affecting our business. These forward looking statements and other forward-looking statements made elsewhere in this document are made under the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. Please read the section titled "Risk Factors" in "Item One – Business" to review certain conditions, among others, which we believe could cause results to differ materially from those contemplated by the forward-looking statements.

Except for historical information contained in this report, the matters discussed are forward-looking statements that involve risks and uncertainties. When used in this report, words such as "anticipates", "believes", "could", "estimates", "expects", "may", "plans", "potential", "intends", and similar expressions, as they relate to the Company or its management identify forward-looking statements. Such forward-looking statements are based on the beliefs of the Company's management, as well as assumptions made by and information currently available to the Company's management.

Among the factors that could cause actual results to differ materially are the following: the effect of business and economic conditions; the effect of the dramatic changes taking place in the healthcare environment; the impact of competitive procedures and products and their pricing; medical insurance reimbursement policies; unexpected manufacturing or supplier problems; unforeseen difficulties and delays in the conduct of clinical trials and other product development programs; the actions of regulatory authorities and third-party payers in the United States and overseas; uncertainties about the acceptance of a novel therapeutic modality by the medical community; continuation of the GEHC agreement; and the risk factors reported from time to time in the Company's SEC reports. The Company undertakes no obligation to update forward-looking statements as a result of future events or developments.

The following discussion should be read in conjunction with the financial statements and notes thereto included in this Transition Report on Form 10-K.

Overview

Vasomedical, Inc. was incorporated in Delaware in July 1987. Unless the context requires otherwise, all references to “we”, “our”, “us”, “Company”, “registrant”, “Vasomedical” or “management” refer to Vasomedical, Inc. and its subsidiaries. Since 1995, we have been primarily engaged in designing, manufacturing, marketing and supporting EECP® Enhanced External Counterpulsation systems, based on our unique proprietary technology, to physicians and hospitals throughout the United States and in select international markets.

In 2010, the Company, through its wholly-owned subsidiary Vaso Diagnostics d/b/a VasoHealthcare, organized a group of medical device sales professionals and entered into the sales representation business as the exclusive representative for the sale of select General Electric Company (GE) diagnostic imaging equipment to specific market segments in the 48 contiguous states of the United States and the District of Columbia.

In September 2011, the Company acquired two Chinese operating companies; Life Enhancement Technologies Ltd and Biox Instruments Co. Ltd to expand its technical and manufacturing capabilities and to enhance its distribution network, technology, and product portfolio. Also in September 2011, the Company restructured to further align its business management structure and long-term growth strategy and will operate through three wholly-owned subsidiaries. Vaso Diagnostics d/b/a VasoHealthcare will continue as an operating subsidiary for the sales representation of GE diagnostic imaging products; Vasomedical Global Corp. will operate the Company’s newly-acquired Chinese companies; and Vasomedical Solutions, Inc. was formed to manage and coordinate our EECP® therapy business as well as other medical equipment operations.

We have achieved profitability through the operation of the VasoHealthcare business. The Company will seek to achieve greater profitability through our recent accretive acquisition of the two Chinese medical device companies and by expanding our U.S. market portfolio. In addition, the Company plans to actively pursue other accretive acquisitions in the international market and is in preliminary discussions to secure a credit facility for up to \$25 million to be utilized for this purpose.

Results of Operations – For the Seven Months Ended December 31, 2011 and 2010

Net revenues increased by \$14,748,000, or 169%, to \$23,489,000 in the seven months ended December 31, 2011, from \$8,741,000 in the seven months ended December 31, 2010. We reported net income applicable to common stockholders of \$3,891,000 in the seven months ended December 31, 2011 as compared to a loss of \$2,604,000 in the seven months ended December 31, 2010. Our total net income (loss) was \$0.03 and \$(0.02) per basic and diluted common share for the seven months ended December 31, 2011 and 2010, respectively.

Revenues

Revenue in our Equipment segment decreased 23% to \$2,576,000, including \$413,000 in FGE revenue, for the seven months ended December 31, 2011 from \$3,328,000 for the seven months ended December 31, 2010. Equipment segment revenue from equipment sales decreased approximately 27% to \$1,473,000 for the seven months ended December 31, 2011 as compared to \$2,025,000 for the seven months ended December 31, 2010. The decrease in equipment sales is due primarily to a 59% decrease in the number of EECP® units sold internationally, coupled with a minor reduction in average selling price, as well as a 10% reduction in domestic sales driven mainly by lower average selling prices on certain used systems shipped. In addition, excluding FGE sales, revenue from other medical equipment increased 18% in the seven months ended December 31, 2011 as compared to the seven months ended December 31, 2010.

We anticipate that demand for EEC[®] systems will remain soft domestically unless there is greater clinical acceptance for the use of EEC[®] therapy in treating patients with angina or angina equivalent symptoms who meet the current reimbursement guidelines, or a favorable change in current reimbursement policies by CMS or third party payors to consider EEC[®] therapy as a first-line treatment option for angina or cover some or all Class II & III heart failure patients. Patients with angina or angina equivalent symptoms eligible for reimbursement under current policies include many with serious comorbidities, such as heart failure, diabetes, peripheral vascular disease and/or others.

Equipment segment revenue from equipment rental and services decreased 15% to \$1,103,000 in the seven months ended December 31, 2011 from \$1,304,000 in the seven months ended December 31, 2010. Revenue from equipment rental and services represented 43% of total Equipment segment revenue in the seven months ended December 31, 2011 and 39% in the seven months ended December 31, 2010. The decrease in revenue generated from equipment rentals and services is due primarily to decreased field service and recognized service contract revenues.

Commission revenues in the Sales Representation segment were \$20,913,000 in the seven months ended December 31, 2011, compared to \$5,413,000 in the seven months ended December 31, 2010. As discussed in Note B, the Company defers recognition of commission revenue until underlying equipment acceptance is complete. As of December 31, 2011, \$14,085,000 in deferred commission revenue was recorded in the Company's consolidated condensed balance sheet, of which \$5,378,000 is long-term.

Gross Profit

The Company recorded gross profit of \$16,756,000, or 71% of revenue, in the seven months ended December 31, 2011 compared to \$5,820,000, or 67% of revenue, in the seven months ended December 31, 2010. The increase of \$10,936,000 was due primarily to higher revenue in the Sales Representation segment, partially offset by lower gross profit rates resulting from higher commission expense..

Equipment segment gross profit decreased to \$1,243,000, or 48% of Equipment segment revenues, for the seven months ended December 31, 2011 compared to \$1,532,000, or 46% of Equipment segment revenues, for the seven months ended December 31, 2010 due mainly to lower sales volume. The decrease in absolute dollars was partially offset by an increase in gross profit percentage, which arose primarily from the inclusion of higher margins on FGE sales. Equipment segment gross profits are dependent on a number of factors, particularly the mix of new and refurbished EEC[®] systems and the mix of models sold, their respective average selling prices, the ongoing costs of servicing EEC[®] systems, and certain fixed period costs, including facilities, payroll and insurance.

Sales Representation segment gross profit was \$15,513,000 for the seven months ended December 31, 2011. Cost of commissions of \$5,400,000 reflects commission expense associated with recognized commission revenues. Commission expense associated with deferred revenue is recorded as deferred commission expense until the related commission revenue is earned.

Operating Income

Operating income was \$5,189,000 for the seven months ended December 31, 2011 as compared to an operating loss of \$2,445,000 for the seven months ended December 31, 2010. The change from an operating loss to operating income was primarily attributable to operating income of \$7,417,000 in our Sales Representation segment for the seven months ended December 31, 2011, as compared to an operating loss of \$2,234,000 for the seven months ended December 31, 2010 in that segment. The 2010 segment loss reflects additional start-up costs and the deferral of commission revenue and expense in the seven months ended December 31, 2010. Equipment segment operating loss in the seven months ended December 31, 2011 was \$1,603,000, including \$578,000 in shared-based expenses, as compared to an operating loss of \$59,000, including \$226,000 in shared-based expenses, in the seven months ended December 31, 2010. The increase in operating loss was primarily due to lower gross profit and higher SG&A costs.

Selling, general and administrative (“SG&A”) expenses for the seven months ended December 31, 2011 and 2010 were \$11,243,000, or 48% of revenues, and \$8,004,000, or 92% of revenues, respectively, reflecting an increase of \$3,239,000 or approximately 40%. The increase in SG&A expenditures in the seven months ended December 31, 2011 resulted primarily from increased wages, benefits, travel, and insurance expenses related to the Sales Representation segment, which was in its start-up phase during the seven months ended December 31, 2010. SG&A also increased in the Equipment segment due to higher sales and marketing expenses mainly related to reimbursement consulting, and the inclusion of FGE costs, as well as higher corporate expenses, mainly accounting, legal and director’s fees.

During the seven months ended December 31, 2011, the Company recorded a provision for doubtful accounts and commission adjustments of \$866,000 as compared to the seven months ended December 31, 2010 when the Company recorded a provision for doubtful accounts and commission adjustments of \$1,150,000. Of the seven months ended December 31, 2011 provision, \$55,000 was to accrue for bad debt expense and \$811,000 was to reduce gross deferred revenues for estimated adjustments.

Research and development (“R&D”) expenses of \$324,000, or 1% of revenues, for the seven months ended December 31, 2011 increased by \$63,000, or 24%, from \$261,000, or 3% of revenues, for the seven months ended December 31, 2010. The increase is primarily attributable to an increase in clinical research expenses.

Interest and Financing Costs

Interest and financing costs for the seven months ended December 31, 2011 was \$9,000 compared to \$8,000 in the seven months ended December 31, 2010. Interest and financing costs consisted of interest on a short-term note to finance the Company’s insurance premiums and interest charged on trade payable to related party.

Interest and Other Income, Net

Interest and other income for the seven months ended December 31, 2011 and 2010, were \$177,000 and \$17,000, respectively. In the seven months ended December 31, 2011 other income primarily consisted of a government grant obtained by one of the Company’s Chinese companies. Interest income reflects interest earned on the Company’s cash balances and financing receivables.

Amortization of Deferred Gain on Sale-leaseback of Building

The amortization of deferred gain on sale-leaseback of building for the seven months ended December 31, 2011 and 2010 was \$31,000. The gain resulted from the Company’s sale-leaseback of its facility.

Income Tax Benefit (Expense), Net

During the seven months ended December 31, 2011, we recorded income tax expense of \$276,000 compared to the seven months ended December 31, 2010, when the Company recorded an income tax expense of \$8,000. The Company utilized \$6.1 million in net reporting loss carryforwards for the seven month period ended December 31, 2011. Income tax expense increased mainly due to Federal Alternative Minimum Tax liability and certain state tax liabilities in excess of net operating loss carryforwards.

Ultimate realization of any or all of the deferred tax assets is not assured due to significant uncertainties and material assumptions associated with estimates of future taxable income during the carry-forward period. The Company believes it is premature to recognize additional deferred tax assets based on such uncertainties. However, such assessments may change as the representation business of VasoHealthcare matures.

Results of Operations – Fiscal Years Ended May 31, 2011 and 2010

Net revenues increased by \$12,167,000, or 289%, to \$16,373,000 in fiscal 2011, from \$4,206,000 in fiscal 2010. We reported a net loss applicable to common stockholders of \$4,320,000 in fiscal 2011 as compared to \$1,892,000 in fiscal 2010. Our total net loss was \$0.04 and \$0.02 per basic and diluted common share for the years ended May 31, 2011 and 2010, respectively.

Revenues

Revenue in our Equipment segment increased 25% to \$5,260,000 for the fiscal year ended May 31, 2011 from \$4,206,000 for the fiscal year ended May 31, 2010. Equipment segment revenue from equipment sales increased approximately 43% to \$3,029,000 for fiscal 2011 as compared to \$2,119,000 for fiscal 2010. The increase in equipment sales is due primarily to a 55% increase in the number of EECP® units sold internationally, as well as a 33% increase in domestic EECP® units shipped. In addition, revenue from other medical equipment increased 363% in fiscal year 2011 as compared to the prior fiscal year.

Average selling prices for EECP equipment were slightly higher in fiscal 2011. We anticipate that demand for EECP® systems would remain soft domestically unless there is greater clinical acceptance for the use of EECP® therapy in treating patients with angina or angina equivalent symptoms who meet the current reimbursement guidelines, or a favorable change in current reimbursement policies by CMS or third party payors to consider EECP therapy as a first-line treatment option for angina or cover some or all Class II & III heart failure patients. Patients with angina or angina equivalent symptoms eligible for reimbursement under current policies include many with serious comorbidities, such as heart failure, diabetes, peripheral vascular disease and/or others.

Equipment segment revenue from equipment rental and services increased 7% to \$2,231,000 in fiscal 2011 from \$2,087,000 in fiscal year 2010. Revenue from equipment rental and services represented 42% of total Equipment segment revenue in fiscal 2011 and 50% in fiscal 2010. The increase in revenue generated from equipment rentals and services is due primarily to increased on-demand service and equipment rental revenues.

Commission revenues in the Sales Representation segment were \$11,113,000 in fiscal 2011. No revenues were recorded in fiscal 2010 as the GEHC contract had not yet begun. As discussed in Note B, the Company defers recognition of commission revenue until underlying equipment acceptance is complete. As of May 31, 2011, \$10,806,000 in deferred commission revenue was recorded in the Company's consolidated condensed balance sheet, of which \$756,000 is long-term.

Gross Profit

The Company recorded gross profit of \$10,912,000, or 67% of revenue, in fiscal 2011 compared to \$2,212,000, or 53% of revenue, in fiscal 2010. The increase of \$8,701,000 was due primarily to both higher gross profit rates and higher absolute dollars in the Sales Representation segment.

Equipment segment gross profit increased to \$2,413,000, or 46% of Equipment segment revenues, for fiscal 2011 compared to \$2,212,000, or 53% of Equipment segment revenues, for fiscal 2010 due mainly to higher sales volume. The increase in absolute dollars was partially offset by a decrease in gross profit percentage, which arose primarily from higher manufacturing overhead costs, including personnel and transportation charges. Equipment segment gross profits are dependent on a number of factors, particularly the mix of new and refurbished EECP® systems and the mix of models sold, their respective average selling prices, the ongoing costs of servicing EECP® systems, and certain fixed period costs, including facilities, payroll and insurance.

Sales Representation segment gross profit was \$8,499,000 for fiscal 2011. Cost of commissions of \$2,614,000 reflects commission expense associated with recognized commission revenues. Commission expense associated with deferred revenue is recorded as deferred commission expense until the related commission revenue is earned.

Operating Loss

Operating loss was \$3,933,000 for fiscal 2011 as compared to an operating loss of \$1,980,000 for fiscal 2010. The increase in the operating loss was primarily attributable to an operating loss of \$2,962,000 in our Sales Representation

segment for fiscal 2011, as compared to an operating loss of \$1,057,000 for fiscal 2010 in that segment. The increased segment loss reflects additional start-up costs and the deferral of commission revenue and expense in fiscal 2011. Equipment segment operating loss in fiscal 2011 was \$525,000, including \$309,000 in shared-based expenses, as compared to an operating loss of \$490,000, including \$55,000 in shared-based expenses, in fiscal 2010.

Selling, general and administrative (“SG&A”) expenses for fiscal 2011 and 2010 were \$14,383,000, or 88% of revenues, and \$3,773,000, or 90% of revenues, respectively, reflecting an increase of \$10,610,000 or approximately 281%. The increase in SG&A expenditures in fiscal 2011 resulted primarily from increased wages, benefits, commissions, and insurance expenses related to the Sales Representation segment, which began operations in the last two months of fiscal 2010 and ramped up in early fiscal 2011.

During fiscal 2011, the Company recorded a provision for doubtful accounts and commission adjustments of \$1,150,000 as compared to fiscal year 2010 when the Company recorded a provision for doubtful accounts and commission adjustments of \$71,000. Of the fiscal 2011 provision, \$1,000 was to reverse the accrual for bad debt expense, \$58,000 were direct write-offs, net of recovery, and \$1,209,000 was to reduce gross deferred revenues for estimated adjustments.

Research and development (“R&D”) expenses of \$462,000, or 3% of revenues, for fiscal 2011 increased by \$43,000, or 10%, from \$419,000, or 10% of revenues, for fiscal 2010. The increase is primarily attributable to an increase in product development expenses.

Interest and Financing Costs

Interest and financing costs for fiscal 2011 was \$32,000 compared to \$5,000 in fiscal 2010. Interest and financing costs consisted of interest on a short-term note to finance the Company’s insurance premiums and interest charged on trade payable to related party.

Interest and Other Income, Net

Interest and other income for fiscal 2011 and 2010, were \$28,000 and \$80,000, respectively. In fiscal year 2010 other income primarily consisted of a cash settlement of a lawsuit against one of the Company’s competitors. Interest income reflects interest earned on the Company’s cash balances and financing receivables.

Amortization of Deferred Gain on Sale-leaseback of Building

The amortization of deferred gain on sale-leaseback of building for fiscal years 2011 and 2010 was \$53,000. The gain resulted from the Company’s sale-leaseback of its facility.

Income Tax Benefit/(Expense), Net

During fiscal year 2011, we recorded income tax expense of \$7,000 compared to fiscal year 2010, when the Company recorded an income tax benefit of \$36,000. The fiscal 2010 income tax benefit was primarily a research and development credit associated with the federal stimulus package of 2009.

Ultimate realization of any or all of the deferred tax assets is not assured due to significant uncertainties and material assumptions associated with estimates of future taxable income during the carry-forward period. In the future, such assessments may change due to the introduction of the distribution and representation business of VasoHealthcare.

Liquidity and Capital Resources

Cash and Cash Flow – For the Seven Months ended December 31, 2011

We have financed our operations primarily from working capital. At December 31, 2011, we had cash and cash equivalents of \$2,294,000, short-term investments of \$110,000 and working capital of \$11,354,000.

Cash used in operating activities was \$5,103,000 during the seven months ended December 31, 2011, which consisted of net income after adjustments to reconcile net income to net cash of \$6,745,000, and cash used by operating assets and liabilities of \$11,848,000. The changes in the account balances primarily reflect increases in other assets of \$1,074,000 and accounts and other receivables of \$16,986,000, partially offset by an increase in accrued commissions of \$1,925,000, and deferred revenue of \$3,305,000. These changes in account balances are due mainly to the operations of our Sales Representation segment. At March 31, 2012 the Company’s cash balances were approximately

\$12.5 million.

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Standard payment terms on our domestic equipment sales are generally net 30 to 90 days from shipment and do not contain “right of return” provisions. We have historically offered a variety of extended payment terms, including sales-type leases, in certain situations and to certain customers in order to expand the market for our EEC[®] products in the US and internationally. Such extended payment terms were offered in lieu of price concessions, in competitive situations, when opening new markets or geographies and for repeat customers. Extended payment terms cover a variety of negotiated terms, including payment in full - net 120, net 180 days or some fixed or variable monthly payment amount for a six to twelve month period followed by a balloon payment, if applicable. During the seven months ended December 31 2011 and 2010, there were \$210,000 and \$0, respectively, in revenues generated from sales in which initial payment terms were greater than 90 days. During the seven months ended December 31, 2011 one sales-type lease with a period of three years generated \$2,000 in interest income. During the seven months ended December 31, 2010, one sales-type lease with a period of three years generated \$42,000 in revenue and \$1,000 in interest income. In general, reserves are calculated on a formula basis considering factors such as the aging of the receivables, time past due, and the customer’s credit history and their current financial status. In most instances where reserves are required, or accounts are ultimately written-off, customers have been unable to successfully implement their EEC[®] program. As we are creating a new market for the EEC[®] therapy and recognizing the challenges that some customers may encounter, we have opted, at times, on a customer-by-customer basis, to recover our equipment instead of pursuing other legal remedies, which has resulted in our recording of a reserve or a write-off.

Investing activities during the seven months ended December 31, 2011 used cash of \$638,000, mainly related to the acquisition of FGE.

Financing activities during the seven months ended December 31, 2011 used cash of \$95,000 for the repayment of notes payable to a related party.

Liquidity

While the Company has achieved substantial profitability for the seven months ended December 31, 2011, it has historically incurred operating losses. We have achieved profitability through the operations of the VasoHealthcare business. The Company will seek to achieve greater profitability through our recent accretive acquisition of the two Chinese medical device companies and by expanding our U.S. market product portfolio to include ambulatory monitoring devices (the BIOX series ECG Holter recorders, ambulatory blood pressure monitors and analysis software) and patient management devices (the EZ ECG and EZ O2 products). In addition, the Company plans to pursue other accretive acquisitions in the international market and is in preliminary discussions to secure a credit facility for up to \$25 million to be utilized for this purpose.

While we expect to continue to generate significant operating cash flows in fiscal 2012, the progressive nature of the GEHC Agreement can cause related cash inflows to vary widely during the year.

Based on our current operations through December 31, 2011, we believe internally generated funds from our Equipment and Sales Representation segments will be sufficient for the Company to continue operations through at least January 1, 2013.

Off-Balance Sheet Arrangements

We do not participate in transactions that generate relationships with unconsolidated entities or financial partnerships, such as entities often referred to as structured finance or special purpose entities (SPES), which would have been established for the purpose of facilitating off-balance sheet arrangements or other contractually narrow or limited purposes. As of December 31, 2011, we are not involved in any unconsolidated SPES.

Related Party Transactions

On February 28, 2011, David Lieberman and Edgar Rios were appointed by the Board of Directors as directors of the Company. Mr. Lieberman, a practicing attorney in the State of New York for in excess of 35 years specializing in corporation and securities law, was appointed to serve as the Vice Chairman of the Board. He is currently a senior partner at the law firm of Beckman, Lieberman & Barandes, LLP, which firm performs certain legal services for the Company. Mr. Rios currently is President of Edgery Consultants, LLC, and was appointed in conjunction with the Company's consulting agreement with Edgery Consultants, LLC.

The consulting agreement (the “Agreement”) between Vasomedical, Inc. and Edgery Consultants, LLC (“Consultant”) commenced on March 1, 2011 and terminates on February 28, 2013. The Agreement provides for the engagement of Consultant to assist the Company in seeking broader reimbursement coverage of EEC[®] therapy. More specifically, Consultant will be assisting the Company in the following areas:

1. Engaging the adoption of EEC[®] therapy as a first line option for FDA cleared indications as it relates to CCS Class III/IV angina with a major commercial healthcare third-party payer.
2. Engaging a major commercial healthcare payer to formally collaborate and co-sponsor a study with Vasomedical for the efficacy, efficiency and/or cost effectiveness of the EEC[®] therapy for NYHA Class II/III heart failure.
3. Engaging final approval from the Centers for Medicare and Medicaid Services (“CMS”) of EEC[®] therapy as a first line treatment for CCS Class III/IV angina.
4. Engaging final approval from CMS to extend coverage and provide for the reimbursement of EEC[®] therapy for CCS Class II angina; and
5. Engaging final approval from CMS to extend coverage and provide for the reimbursement of EEC[®] therapy for NYHA Class II/III heart failure.

In consideration for the services to be provided by Consultant under the Agreement, the Company has agreed to issue to Consultant or its designees, approximately 10% of the outstanding capital stock of the Company, of which the substantial portion (in excess of 82%) is performance based as referenced above. In conjunction with the Agreement, 3,000,000 shares of restricted common stock valued at \$1,020,000 were issued in March 2011. In connection with this Agreement, Mr. Lieberman received 600,000 of these restricted shares. The Company has recorded the fair value of the shares issued to Consultant as a prepaid expense and is amortizing the cost ratably over the two year agreement. The unamortized value is reported as Deferred Related Party Consulting Expense in our accompanying consolidated balance sheet as of December 31, 2011.

Through the Company’s acquisition of FGE in September 2011, it assumed the liability for \$288,000 in unsecured notes payable to the President of LET and his spouse, of which \$95,000 was repaid in December 2011, and \$190,000, bearing interest at 6% per annum, matured March 31, 2012. In addition, \$10,000 in pre-acquisition earnings were distributed to current BIOX management and during the seven months ended December 31, 2011. The Company also recorded \$196,000 in loans and advances made to officers of FGE during the seven months ended December 31, 2011. These loans are short term and do not bear interest.

Effects of Inflation

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

Critical Accounting Policies and Estimates

Note B of the Notes to Consolidated Financial Statements includes a summary of our significant accounting policies and methods used in the preparation of our financial statements. In preparing these financial statements, we have made our best estimates and judgments of certain amounts included in the financial statements, giving due consideration to materiality. The application of these accounting policies involves the exercise of judgment and use of assumptions as to future uncertainties and, as a result, actual results could differ from these estimates. Our critical accounting policies are as follows:

Revenue Recognition

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

In most cases, revenue from domestic EECP® system sales is generated from multiple-element arrangements that require judgment in the areas of customer acceptance, collectability, the separability of units of accounting, and the fair value of individual elements. We follow the FASB Accounting Standards Codification (“ASC”) Topic 605 “Revenue Recognized” (“ASC 605”) which outlines a framework for recognizing revenue from multi-deliverable arrangements. The principles and guidance outlined in ASC 605 provide a framework to determine (a) how the arrangement consideration should be measured (b) whether the arrangement should be divided into separate units of accounting, and (c) how the arrangement consideration should be allocated among the separate units of accounting. We determined that the domestic sale of our EECP® systems includes a combination of three elements that qualify as separate units of accounting:

- EECP® equipment sale;
- provision of in-service and training support consisting of equipment set-up and training provided at the customer’s facilities; and
- a service arrangement (usually one year), consisting of: service by factory-trained service representatives, material and labor costs, emergency and remedial service visits, software upgrades, technical phone support and preferred response times.

Each of these elements represent individual units of accounting as the delivered item has value to a customer on a stand-alone basis, objective and reliable evidence of fair value exists for undelivered items, and arrangements normally do not contain a general right of return relative to the delivered item. We determine fair value based on the price of the deliverable when it is sold separately, or based on third-party evidence, or based on estimated selling price. Assuming all other criteria for revenue recognition have been met, we recognize revenue for:

- EECP® equipment sales, when delivery and acceptance occurs based on delivery and acceptance documentation received from independent shipping companies or customers;
 - in-service and training, following documented completion of the training; and
 - service arrangement, ratably over the service period, which is generally one year.

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

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

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

Revenue and Expense Recognition for VasoHealthcare

The Company recognizes commission revenue in its Sales Representation segment when persuasive evidence of an arrangement exists, service has been rendered, the price is fixed or determinable and collectability is reasonably assured. These conditions are deemed to be met when the underlying equipment has been accepted at the customer site in accordance with the specific terms of the sales agreement. Consequently, amounts billable under the agreement with GE Healthcare in advance of the customer acceptance of the equipment are recorded as accounts receivable and deferred revenue in the consolidated condensed balance sheet. Similarly, commissions payable to our sales force related to such billings are recorded as deferred commission expense when the associated deferred revenue is recorded. Commission expense is recognized when the corresponding commission revenue is recognized.

Accounts Receivable, net

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

Inventories, net

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

We comply with the provisions of ASC Topic 330, "Inventory". The statement clarifies that abnormal amounts of idle facility expense, freight, handling costs, and wasted materials (spoilage) should be recognized as current-period charges and requires the allocation of fixed production overheads to inventory based on the normal capacity of the production facilities.

Deferred Revenues

The Company records revenue on extended service contracts ratably over the term of the related contract period. In accordance with the provisions of ASC Topic 605, we defer revenue related to EECP® system sales for the fair value of installation and in-service training to the period when the services are rendered and for warranty obligations ratably over the service period, which is generally one year.

Amounts billable under the agreement with GE Healthcare in advance of customer acceptance of the equipment are recorded initially as deferred revenue, and commission revenue is subsequently recognized as customer acceptance of such equipment is reported to us by GEHC.

Warranty Costs

Equipment sold is generally covered by a warranty period of one year. Under the provisions of ASC Topic 605, for certain arrangements, a portion of the overall system price attributable to the first year service arrangement is deferred and recognized as revenue over the service period. As such, we do not accrue warranty costs upon delivery but rather we recognize warranty and related service costs as incurred.

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

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

Net Income (Loss) per Common Share

Basic income (loss) per share is based on the weighted average number of common shares outstanding without consideration of potential common stock. Diluted income (loss) per share is based on the weighted number of common and potential dilutive common shares outstanding. The calculation takes into account the shares that may be issued upon the exercise of stock options and warrants, reduced by the shares that may be repurchased with the funds received from the exercise, based on the average price during the period. Options and warrants to purchase shares of common stock, as well as convertible preferred stock and unvested common stock grants, are excluded from the computation of diluted earnings per share because the effect of their inclusion would be anti-dilutive.

Income Taxes

Deferred income taxes are recognized for temporary differences between financial statement and income tax bases of assets and liabilities and loss carry forwards for which income tax benefits are expected to be realized in future years. A valuation allowance is established, when necessary, to reduce deferred tax assets to the amount expected to be realized. In estimating future tax consequences, we generally consider all expected future events other than an enactment of changes in the tax laws or rates. Deferred tax assets are continually evaluated for realizability. To the extent our judgment regarding the realization of the deferred tax assets changes, an adjustment to the allowance is recorded, with an offsetting increase or decrease, as appropriate, in income tax expense. Such adjustments are recorded in the period in which our estimate as to the realizability of the assets changed that it is “more likely than not” that all of the deferred tax assets will be realized. The “more likely than not” standard is subjective and is based upon our estimate of a greater than 50% probability that the deferred tax asset will be realized.

Deferred tax assets and liabilities are classified as current or non-current based on the classification of the related asset or liability for financial reporting. A deferred tax asset or liability that is not related to an asset or liability for financial reporting, including deferred tax assets related to carryforwards, are classified according to the expected reversal date of the temporary difference.

The Company also complies with the provisions of the ASC Topic 740, “Income Taxes”, which prescribes a recognition threshold and a measurement attribute for the financial statement recognition and measurement of tax positions taken or expected to be taken in a tax return. For those benefits to be recognized, a tax position must be more-likely-than-not to be sustained upon examination by taxing authorities. Based on its analysis, except for certain liabilities assumed in the FGE acquisition, the Company has determined that it has not incurred any liability for unrecognized tax benefits as of December 31, 2011, May 31, 2011 and May 31, 2010. The Company recognizes accrued interest and penalties related to unrecognized tax benefits as income tax expense. No amounts were accrued for the payment of interest and penalties at December 31, 2011, May 31, 2011 and May 31, 2010. Management is currently unaware of any issues under review that could result in significant payments, accruals or material deviations from its position.

Share-based Employee Compensation

The Company complies with ASC Topic 718 “Compensation – Stock Compensation” (“ASC 718”), which requires all companies to recognize the cost of services received in exchange for equity instruments, to be recognized in the

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

Vasomedical accounts for share-based compensation in accordance with fair value recognition provisions, under which the Company uses the Black-Scholes option pricing model which requires the input of subjective assumptions. These assumptions include estimating the length of time employees will retain their stock options before exercising them (“expected term”), the estimated volatility of the Company’s common stock price over the expected term and the number of options that will ultimately not complete their vesting requirements. The Company estimates the expected term and forfeitures based on the terms set forth in the option agreements and no assumption that any options will not complete their vesting period, which approximates actual historical behavior, and it estimates volatility of the Company’s stock based on the Company’s historical stock price performance over the past five years. Changes in the subjective assumptions could materially affect the estimate of fair value of stock-based compensation; however management believes changes in certain assumptions that could be reasonably possible in the near term, would not have a material effect on the expense recognized for fiscal 2011.

Equity instruments issued to non-employees in exchange for goods, fees and services are accounted for under the fair value-based method of ASC Topic 505 “Equity” (ASC 505).

Recently Issued Accounting Pronouncements

Adoption of New Standards

Other Comprehensive Income: Presentation of Comprehensive Income

In June 2011, new guidance was issued that amends the current comprehensive income guidance. The new guidance allows the option to present the total of comprehensive income, the components of net income, and the components of other comprehensive income either in a single or continuous statement of comprehensive income or in two separate but consecutive statements. The amendments in this update do not change the items that must be reported in other comprehensive income or when an item of other comprehensive income must be reclassified to net income. The new guidance is to be applied retrospectively and is effective for fiscal years, and interim periods, beginning after December 15, 2011, with early adoption permitted. The Company has elected early adoption of this guidance and does not expect that it will have a material impact on the Company’s consolidated financial statements.

Intangibles—Goodwill and Other: Testing Goodwill for Impairment

In September 2011, an accounting standard update regarding testing of goodwill for impairment was issued. This standard update gives companies the option to perform a qualitative assessment to first assess whether the fair value of a reporting unit is less than its carrying amount. If an entity determines it is not more likely than not that the fair value of the reporting unit is less than its carrying amount, then performing the two-step impairment test is unnecessary. The new guidance is to be applied prospectively effective for annual and interim goodwill impairment tests beginning after December 15, 2011, with early adoption permitted. The Company has elected early adoption of this guidance and does not expect that it will have a material impact on the Company’s consolidated financial statements.

ITEM 8 - FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

The consolidated financial statements listed in the accompanying Index to Consolidated Financial Statements are filed as part of this report.

ITEM 9A - CONTROLS AND PROCEDURES

Report on Disclosure Controls and Procedures

Disclosure controls and procedures reporting as promulgated under the Exchange Act is defined as controls and procedures that are designed to ensure that information required to be disclosed by us in the reports that we file or submit under the Exchange Act are recorded, processed, summarized and reported within the time periods specified in the SEC rules and forms. Disclosure controls and procedures include without limitation, controls and procedures designed to ensure that information required to be disclosed by us in the reports that we file or submit under the Exchange Act is accumulated and communicated to our management, including our Chief Executive Officer (“CEO”) and Chief Financial Officer (“CFO”), or persons performing similar functions, as appropriate to allow timely decisions regarding required disclosure.

Our CEO and our CFO have evaluated the effectiveness of the design and operation of our disclosure controls and procedures as of December 31, 2011 and have concluded that the Company’s disclosure controls and procedures were not effective as of December 31, 2011 due to the deficiencies described in Management’s Report on Internal Control

over Financial Reporting below. The Company intends to engage additional accounting personnel, including an accounting controller, and strengthen its internal controls with regard to its closing process, related disclosures, and the approval of certain transactions.

Management's Report on Internal Control over Financial Reporting

Management is responsible for establishing and maintaining adequate internal control over financial reporting for the Company as defined in Rule 13a-15(f) of the Exchange Act. Internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial statements for external purposes in accordance with accounting principles generally accepted in the United States of America. Internal control involves maintaining records that accurately represent our business transactions, providing reasonable assurance that receipts and expenditures of company assets are made in accordance with management authorization, and providing reasonable assurance that unauthorized acquisition, use or disposition of company assets that could have a material effect on our financial statements would be detected or prevented on a timely basis.

Because of its innate limitations, internal control over our financial statements is not intended to provide absolute guarantee that a misstatement can be detected or prevented on the statements. Therefore, even those systems determined to be effective can provide only reasonable assurance with respect to financial statement preparation and presentation. Also projections of any evaluation of effectiveness to future periods are subject to risk that controls may become inadequate because of changes in condition, or that the degree of compliance with the policies or procedures may deteriorate.

Management conducted an evaluation of the effectiveness of our internal control over financial reporting based on the framework in Internal Control – Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). A material weakness is a deficiency, or combination of deficiencies, in internal control over financial reporting, such that there is a reasonable possibility that a material misstatement of the Company's annual or interim financial statements will not be prevented or detected on a timely basis.

Based on this evaluation and those criteria, the Company's CEO and CFO concluded that the Company's internal control over financial reporting was not effective as of December 31, 2011, due to the following deficiencies at the Company's Fast Growth Enterprises (FGE) subsidiary and at the two Chinese operating companies FGE owns or controls:

- Insufficient controls and management review over the recording of certain transactions.
- Lack of accounting personnel with appropriate level of knowledge and experience in accounting principles generally accepted in the United States of America and related accounting systems and closing process.

This report does not include an attestation report of the Company's Independent Registered Public Accounting Firm regarding internal control over financial reporting. Management's report was not subject to attestation by the Company's Independent Registered Public Accounting Firm pursuant to temporary rules of the Securities and Exchange Commission that permit the Company to provide only Management's report in this Transition Report.

PART III

ITEM 10 – DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE

Directors of the Registrant

As of April 23, 2012, the members of our Board of Directors are:

| Name of Director | Age | Principal Occupation | Director Since |
|------------------|-----|------------------------------------|----------------|
| Simon Srybnik | 95 | Chairman of the Board and Director | June, 2007 |

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| | | | |
|--------------------------------|----|---|----------------|
| David Lieberman (1) | 67 | Vice Chairman of the Board and Director | February, 2011 |
| Jun Ma | 48 | President, Chief Executive Officer and Director | June, 2007 |
| Behnam Movaseghi (1) (2)(3) | 58 | Director | July, 2007 |
| Edgar Rios | 60 | Director | February, 2011 |
| Peter C. Castle (1) (2)(3) | 43 | Director | August, 2010 |

(1) Member of the Executive Committee, which was formed in January, 2012.

(2) Member of the Audit Committee

(3) Member of Compensation Committee

The following is a brief account of the business experience for at least the past five years of our directors:

Simon Srybnik has been a director since June 2007 and Chairman of the Board since June 2010. He is the Chairman of the Board of Kerns Manufacturing Corp. and Living Data Technology Corp. A lifetime entrepreneur and industrialist, Mr. Srybnik has founded and managed many companies in various industries including machinery and process equipment, aerospace and defense, biotechnology and healthcare.

David Lieberman has been a director of the Company and the Vice Chairman of the Board, since February 2011. Mr. Lieberman has been a practicing attorney in the State of New York for more than 35 years, specializing in corporation and securities law. He is currently a senior partner at the law firm of Beckman, Lieberman & Barandes, LLP, which firm performs certain legal services for the Company. Mr. Lieberman is a former Chairman of the Board of Herley Industries, Inc., which company was sold in March, 2011.

Jun Ma, PhD has been a director since June 2007 and was appointed President and Chief Executive Officer of the Company on October 16, 2008. Dr. Ma has been an associate professor in engineering at New York Institute of Technology since 1997 and an assistant professor from 1993 to 1997. Previously Dr. Ma provided technology and business consulting services to several companies in aerospace, automotive, biomedical, medical device, and other industries, including Kerns Manufacturing Corp. and Living Data Technology Corp., both of which are stockholders of our Company.

Behnam Movaseghi has been a director since July 2007. Mr. Movaseghi has been treasurer of Kerns Manufacturing Corporation since 2000, and controller from 1990 to 2000. For approximately ten years prior thereto Mr. Movaseghi was a tax and financial consultant. Mr. Movaseghi is a Certified Public Accountant.

Edgar G. Rios has been a director of the Company since February 2011. Mr. Rios currently is President of Edgary Consultants, LLC. and was appointed a director in conjunction with the Company's consulting agreement with Edgary Consultants, LLC. Mr. Rios is co-founder and managing director of Wenzel Capital Partners, a venture capital and private equity firm. Mr. Rios was Executive Vice President, General Counsel, Secretary, and Director of AmeriChoice Corporation from its inception in 1989 through its acquisition by UnitedHealthcare in 2002. He is a co-founder of AmeriChoice and was part of the management team that grew revenues to \$675 million in 2001. Prior to co-founding AmeriChoice, Mr. Rios was a co-founder of a number of businesses that provided technology services and non-technology products to government purchasers. Over the years, Mr. Rios also has been an investor, providing seed capital to various technology and nontechnology start-ups. Mr. Rios also serves as a member of the Board of Trustees of Meharry Medical School and as a director and secretary of the An-Bryce Foundation. Mr. Rios holds a J.D. from Columbia University Law School and an A.B. from Princeton University.

Peter Castle has been a director since August 2010. Mr. Castle is currently the President and Chief Operating Officer of NetWolves Corporation, where he has been employed since 1998. Mr. Castle also held the position of Chief Financial Officer from 2001 until October 2009, Vice President of Finance since January 2000, Controller from August 1998 until December 1999 and Treasurer and Secretary from August 1999. NetWolves is a global telecommunications and Internet managed services provider offering single-source network solutions that provides multi-carrier and multi-vendor implementation to over 1,000 customers worldwide.

Committees of the Board of Directors

Executive Committee

The primary purpose of the Executive Committee is to function when the Board of Directors is not in session. During the intervals between meetings of the Board, the Committee shall have and may exercise the powers of the Board, except as limited by Delaware statute. It will also take such other action and do such other things as may be referred to it from time to time by the Board.

Audit Committee and Audit Committee Financial Expert

The Board has a standing Audit Committee. The Board has affirmatively determined that each director who serves on the Audit Committee is independent, as the term is defined by applicable Securities and Exchange Commission ("SEC") rules. During the seven months ended December 31, 2011, ("Transition Period") the Audit Committee consisted of Peter Castle, who has served as the committee chair since August 2010, and Behnam Movaseghi, who joined the committee in November 2011. The members of the Audit Committee have substantial experience in assessing the performance of companies, gained as members of the Company's Board of Directors and Audit Committee, as well as by serving in various capacities in other companies or governmental agencies. As a result, they each have an understanding of financial statements. The Board believes that Peter Castle fulfills the role of the financial expert on this committee.

The Audit Committee regularly meets with our independent registered public accounting firm outside the presence of management.

The Audit Committee operates under a charter approved by the Board of Directors. The Audit Committee charter is available on our website.

Compensation Committee

Our Compensation Committee annually establishes, subject to the approval of the Board of Directors and any applicable employment agreements, the compensation that will be paid to our executive officers during the coming year, as well as administers our stock-based benefit plans. During the seven months ended December 31, 2011, the Compensation Committee consisted of Behnam Movaseghi, who served as the committee chair, and Peter Castle. None of these persons were our officers or employees during the Transition Period or, except as otherwise disclosed, had any relationship requiring disclosure herein.

The Compensation Committee operates under a charter approved by the Board of Directors. The Compensation Committee charter is available on our website.

MEETINGS OF THE BOARD OF DIRECTORS AND COMMITTEES

During the seven months ended December 31, 2011 there were:

- 3 meetings of the Board of Directors
- 2 meetings of the Audit Committee

The Compensation Committee did not hold any meetings during the seven months ended December 31, 2011.

Section 16(a) Beneficial Ownership Reporting Compliance

Section 16(a) of the Exchange Act requires directors, executive officers and persons who beneficially own more than 10% of our common stock (collectively, "Reporting Persons") to file initial reports of ownership and reports of changes in ownership of our common stock with the SEC. Reporting Persons are required by SEC regulations to furnish us with copies of all Section 16(a) reports they file. To our knowledge, based solely on our review of the copies of such reports received or written representations from certain Reporting Persons that no other reports were required, we believe that during the Transition Period, all Reporting Persons timely complied with all applicable filing requirements.

Corporate Governance - Code of Ethics

We have adopted a Corporate Code of Business Ethics (the "Code") that applies to all employees, including our principal executive officer, principal financial officer, and directors of the Company. A copy of the Code can be found on our website, www.vasomedical.com. The Code is broad in scope and is intended to foster honest and ethical conduct, including accurate financial reporting, compliance with laws and the like. If any substantive amendments are made to the Code or if there is any grant of waiver, including any implicit waiver, from a provision of the Code to our Chief Executive Officer or Chief Financial Officer, we will disclose the nature of such amendment or waiver in a Current Report on Form 8-K.

Executive Officers of the Registrant

As of April 23, 2012 our executive officers are:

| Name of Officer | Age | Position held with the Company |
|--------------------|-----|---|
| Jun Ma, PhD | 48 | President, Chief Executive Officer and Director |
| Michael J. Beecher | 67 | |

Jonathan P. Newton

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Chief Financial Officer and
Secretary
Vice President of Finance and
Controller

Michael J. Beecher, CPA, joined the Company as Chief Financial Officer in September 2011. Prior to joining Vasomedical, Mr. Beecher was Chief Financial Officer of Direct Insite Corp., a publicly held company, from December 2003 to September 2011. Prior to his position at Direct Insite, Mr. Beecher was Chief Financial Officer and Treasurer of FiberCore, Inc., a publicly held company in the fiber-optics industry. From 1989 to 1995 he was Vice-President Administration and Finance at the University of Bridgeport. Mr. Beecher began his career in public accounting with Haskins & Sells, an international public accounting firm. He is a graduate of the University of Connecticut, a Certified Public Accountant and a member of the American Institute of Certified Public Accountants.

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Jonathan P. Newton served as Chief Financial Officer of the Company from September 1, 2010 to September 8, 2011, and is currently Vice President of Finance and Controller. From June 2006 to August 2010, Mr. Newton was Director of Budgets and Financial Analysis for Curtiss-Wright Flow Control. Prior to his position at Curtiss-Wright Flow Control, Mr. Newton was Vasomedical's Director of Budgets and Analysis from August 2001 to June 2006. Prior positions included Controller of North American Telecommunications Corp., Accounting Manager for Luitpold Pharmaceuticals, positions of increasing responsibility within the internal audit function of the Northrop Grumman Corporation and approximately three and one half years as an accountant for Deloitte Haskins & Sells, during which time Mr. Newton became a Certified Public Accountant. Mr. Newton holds a B.S. in Accounting from SUNY at Albany, and a B.S. in Mechanical Engineering from Hofstra University.

ITEM 11 - EXECUTIVE COMPENSATION

The following table sets forth the annual and long-term compensation of our Chief Executive Officer and each of our most highly compensated officers and employees who were serving as executive officers or employees at the end of the last completed fiscal year, and certain former executive officers as required under SEC rules (collectively, the "Named Executive Officers") for services rendered for the seven months ended December 31, 2011, the year ended May 31, 2011 ("fiscal 2011"), and the year ended May 31, 2010 ("fiscal 2010").

Summary Compensation Table

| Name and Principal Position | Year | Salary (\$) | Bonus (\$) | Stock Awards (\$)(1) | Option Awards (\$)(1) | Non-Equity Nonqualified Incentive Plan Compensation | | All Other Compensation (\$)(2) | Total (\$) |
|--|-------------------|-------------|------------|----------------------|-----------------------|---|---------------|--------------------------------|------------|
| | | | | | | Deferred Compensation (\$) | Earnings (\$) | | |
| Jun Ma, PhD Chief Executive Officer (3) | Transition Period | 116,667 | - | - | - | - | - | 45,389 | 162,056 |
| | 2011 | 144,046 | - | 105,000 | - | - | - | - | 249,046 |
| | 2010 | 148,471 | - | 25,000 | 20,000 | - | - | - | 193,471 |
| Michael J. Beecher Chief Financial Officer | Transition Period | 52,654 | - | 166,250 | - | - | - | 17,489 | 236,393 |
| Jonathan P. Newton Vice President of Finance and Controller (4) | Transition Period | 81,667 | - | - | - | - | - | 11,411 | 93,078 |
| | 2011 | 105,000 | - | 31,500 | - | - | - | 210 | 136,710 |
| John C. K. Hui (Senior Vice President and Chief Technology Officer) (5) | Transition Period | 93,730 | - | - | - | - | - | 937 | 94,667 |
| | 2011 | 144,209 | - | - | - | - | - | 1,193 | 145,402 |
| | 2010 | 157,151 | - | 20,000 | - | - | - | 886 | 178,037 |
| W. Brent Barron | Transition Period | 158,513 | 29,908 | - | - | - | - | 4,603 | 193,024 |

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| | | | | | | | | | |
|--|------|---------|--------|--------|---|---|---|-----|---------|
| (Chief Operating Officer - VasoHealthcare) | 2011 | 270,000 | 60,750 | 17,100 | - | - | - | 963 | 348,813 |
| (6) | 2010 | 45,000 | - | - | - | - | - | - | 45,000 |
| Tarachand Singh | 2011 | 20,000 | - | - | - | - | - | 220 | 20,220 |
| (Chief Financial Officer) (7) | 2010 | 120,000 | - | - | - | - | - | 960 | 120,960 |

1. Represents fair value on the date of grant. See Note B to the Consolidated Financial Statements included in our Form 10-K for the seven months ended December, 2011 for a discussion of the relevant assumptions used in calculating grant date fair value.
2. Represents tax gross-ups, vehicle allowances, and amounts matched in the Company's 401(k) Plan.
3. Dr. Ma has served as President and Chief Executive Officer since October 16, 2008.
4. Mr. Newton served as Chief Financial Officer from September 1, 2010 to September 8, 2011, and is currently Vice President of Finance and Controller.
5. Dr. Hui was Senior Vice President and Chief Technology Officer from October 16, 2008 to November 14, 2011 and President and Chief Executive Officer from April 30, 2007 to October 15, 2008.
6. Mr. Barron served as Chief Operating Officer of VasoHealthcare from April 1, 2010 to April 5, 2012.
7. Mr. Singh was Chief Financial Officer from March 11, 2009 to August 26, 2010.

Outstanding Equity Awards at Last Fiscal Year End

The following table provides information concerning outstanding options, unvested stock and equity incentive plan awards for our Named Executive Officers at December 31, 2011:

| Name | Option Awards | | | Equity Incentive Plan Awards: | | Stock Awards | | Equity Incentive Plan Awards: | |
|--------------------|---|---|---|-------------------------------|------------------------|---|---|---|---|
| | Number of Securities Underlying Unexercised Options - Exercisable | Number of Securities Underlying Unexercised Options - Unexercisable | Equity Incentive Plan Awards: Number of Unexercised Options | Option Exercise Price | Option Expiration Date | Number of Shares or Units of Stock That Have Not Vested | Market Value of Shares or Units of Stock That Have Not Vested | Unearned Shares, Units or Other Rights That Have Not Vested | Unearned Shares, Units or Other Rights That Have Not Vested |
| Jun Ma, PhD | 150,000 | - | - | \$0.12 | 7/25/2017 | - | - | - | - |
| | 250,000 | - | - | \$0.08 | 12/17/2014 | - | - | - | - |
| | | | | | | 333,333 | \$73,333 | - | - |
| Michael J. Beecher | | | | | | 375,000 | \$82,500 | | |
| Jonathan P. Newton | | | | | | 100,000 | \$22,000 | | |

Employment Agreements

On March 21, 2011, the Company entered into an Employment Agreement with its President and Chief Executive Officer, Jun Ma, for a three-year term ending on March 14, 2014 (the "Agreement"). The Agreement provides for annual compensation of \$200,000. Dr. Ma shall be eligible to receive a bonus for the fiscal year ended May 31, 2011, and for each fiscal year thereafter during the employment term. The amount and the occasion for payment of such bonus, if any, shall be at the discretion of the Board of Directors. Dr. Ma shall also be eligible for an award under any long-term incentive compensation plan and grants of options and awards of shares of the Company's stock, as determined at the Board of Directors' discretion. The Agreement further provides for reimbursement of certain expenses, and certain severance benefits in the event of termination prior to the expiration date of the Agreement.

Pursuant to the terms of his employment agreement with the Company, at the recommendation of the Compensation Committee, the Executive Committee of the Company approved an increase in his annual salary to \$275,000, awarded him a \$50,000 bonus, and awarded him 500,000 restricted shares of common stock, of which one-half vests immediately and the remainder in one year.

401(K) Plan

In April 1997, the Company adopted the Vasomedical, Inc. 401(k) Plan to provide retirement benefits for its employees. As allowed under Section 401(k) of the Internal Revenue Code, the plan provides tax-deferred salary deductions for eligible employees. Employees are eligible to participate in the next quarter enrollment period after employment. Participants may make voluntary contributions to the plan up to 80% of their compensation subject to legal restrictions. In the seven months ended December 31, 2011, and for fiscal years 2011 and 2010, the Company made discretionary contributions of approximately \$25,000, \$29,000 and \$3,000, respectively, to match a percentage of employee contributions.

Director's Compensation

Non-employee directors receive a fee of \$2,500 for each Board of Directors and Committee meeting attended. Committee chairs receive an annual fee of \$5,000. Non-employee directors also receive an annual fee of \$30,000. These fees are either paid in cash, or common stock valued at the fair market value of the common stock on the date of grant, which is the meeting date. During the seven months ended December 31, 2011 the Audit Committee chairman received an additional 50,000 shares.

Director Compensation

| Name | Fees Earned or Paid in Cash (\$) | Stock Awards (\$) | Option Awards (\$) | Non-equity Incentive Plan Compensation (\$) | Nonqualified Deferred Compensation Earnings (\$) | All Other Compensation (\$) | Total (\$) |
|---------------------|--|-------------------------|--------------------------|---|--|-----------------------------------|---------------|
| Simon Srybnik | 9,500 | - | - | - | - | 7,000 | 16,500 |
| Behnam Movaseghi | 10,333 | - | - | - | - | 23,667 | 34,000 |
| William Dempsey | 6,500 | - | - | - | - | 165,853 | 172,353 |
| Peter Castle | 17,833 | 23,500 | - | - | - | 18,333 | 59,666 |
| Edgar Rios | 9,500 | - | - | - | - | 10,333 | 19,833 |
| David Lieberman | 9,500 | - | - | - | - | 10,333 | 19,833 |

Compensation Committee Interlocks and Insider Participation

During the seven months ended December 31, 2011, the Compensation Committee consisted of Behnam Movaseghi, who served as the committee chair, and Peter Castle. None of these persons were our officers or employees during the seven months ended December 31, 2011 or, except as otherwise disclosed, had any relationship requiring disclosure herein.

ITEM 12 - SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS

The following table sets forth the beneficial ownership of shares of our common stock as of April 23, 2012 of (i) each person known by us to beneficially own 5% or more of the shares of outstanding common stock, based solely on filings with the SEC, (ii) each of our executive officers and directors, and (iii) all of our executive officers and directors as a group. Except as otherwise indicated, all shares are beneficially owned, and investment and voting power is held by the persons named as owners. To our knowledge, except under community property laws or as otherwise noted, the persons and entities named in the table have sole voting and sole investment power over their

shares of our common stock. Unless otherwise indicated, each beneficial owner listed below maintains a mailing address of c/o Vasomedical, Inc., 180 Linden Avenue, Westbury, New York 11590.

| Name of Beneficial Owner | Common Stock | |
|---|---------------------------|--------------------------|
| | Beneficially Owned (1) | % of Common Stock (2) |
| Michael J. Beecher ** | 100,000 | * |
| Peter Castle ** | 200,000 | * |
| David Lieberman ** | 1,324,200 | * |
| Jun Ma, PhD ** | 2,545,834 | 1.60 % |
| Benham Movaseghi ** | 1,064,404 | * |
| Jonathan Newton ** | 200,000 | * |
| Edgar Rios ** | 1,475,000 | * |
| Simon Srybnik (3) (4) ** | 55,738,318 | 35.08 % |
| Louis Srybnik (3) (4) | 45,165,993 | 28.45 % |
| ** Directors and executive officers as a group (10 persons) | 62,647,756 | 39.24 % |

*Less than 1% of the Company's common stock

1. No officer or director owns more than one percent of the issued and outstanding common stock of the Company unless otherwise indicated. Includes beneficial ownership of the following numbers of shares that may be acquired within 60 days of April 23, 2012 pursuant to stock options awarded under our stock plans:

| | |
|---|---------|
| Jun Ma, PhD | 400,000 |
| Behnam Movaseghi | 350,000 |
| Simon Srybnik | 150,000 |
| Directors and executive officers as a group | 900,000 |

2. Applicable percentages are based on 158,682,110 shares of common stock outstanding as of April 23, 2012, adjusted as required by rules promulgated by the SEC.
3. Simon Srybnik and his brother Louis Srybnik are the sole directors and the Chairman of the Board and President, respectively of Kerns, which is the record holder of 25,714,286 shares. They are the sole shareholders of Kerns, each holding 50% of the shares. The reporting persons, accordingly, share voting and dispositive powers over the 25,714,286 shares held by Kerns. As a result, they may be deemed to be the co-beneficial owners of an aggregate of 25,714,286 shares. Mr. Simon Srybnik also holds sole dispositive power over 150,000 shares underlying the option he was granted upon being appointed to the Board of Directors, 598,125 shares of common stock awarded him as of December 31, 2011, as well as 11,460,900 additional shares of common stock. Mr. Louis Srybnik holds sole dispositive power over 1,636,700 shares of common stock.
4. Simon Srybnik and his brother Louis Srybnik are the sole directors and officers of Living Data Technology Corporation ("Living Data"). They also each own 35% of the outstanding shares of Living Data. The reporting persons, accordingly, share voting and dispositive powers over the 17,815,007 shares of our common stock owned by Living Data and, as a result, may be deemed to be the co-beneficial owners thereof.

Equity Compensation Plan Information

We maintain various stock plans under which stock options and stock grants are awarded at the discretion of our Board of Directors or its Compensation Committee. The purchase price of the shares under the plans and the shares subject to each option granted is not less than the fair market value on the date of the grant. The term of each option is generally five years and is determined at the time of the grant by our board of directors or the compensation committee. The participants in these plans are officers, directors, employees, and consultants of the Company and its subsidiaries and affiliates.

| Plan category | (a) Number of securities to be issued upon exercise of outstanding options, warrants and rights | (b) Weighted-average exercise price of outstanding options, warrants and rights | (c) Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a)) |
|--|---|---|---|
| Equity Compensation plans approved by security holders | 1,489,776 | \$ 0.17 | 785,224 |
| Equity Compensation plans not approved by security holders (1) | 6,993,214 | \$ 0.11 | 766,008 |
| Total | 8,482,990 | | 1,551,232 |

(1) Includes 4,605,714 shares issuable upon exercise of options and warrants, 62,500 shares issuable under a consulting agreement with a former director, and 2,325,000 shares of restricted common stock granted, but unissued, under the 2010 Plan. The weighted average exercise price of the options and warrants is \$0.11, and the exercise price for the stock grants is zero. 766,008 shares remain available for future grants under the 2010 Plan.

The following information is provided about our current stock plans not approved by stockholders:

1999 Stock Option Plan

In July 1999, the Company's Board of Directors approved the 1999 Stock Option Plan (the 1999 Plan), for which the Company reserved an aggregate of 2,000,000 shares of common stock. The 1999 Plan provides that a committee of the Board of Directors of the Company will administer it and that the committee will have full authority to determine the identity of the recipients of the options and the number of shares subject to each option. Options granted under the 1999 Plan may be either incentive stock options or non-qualified stock options. The option price shall be 100% of the fair market value of the common stock on the date of the grant (or in the case of incentive stock options granted to any individual principal stockholder who owns stock possessing more than 10% of the total combined voting power of all voting stock of the Company, 110% of such fair market value). The term of any option may be fixed by the committee

but in no event shall exceed ten years from the date of grant. Options are exercisable upon payment in full of the exercise price, either in cash or in common stock valued at fair market value on the date of exercise of the option.

In July 2000, the Company's Board of Directors increased the number of shares authorized for issuance under the 1999 Plan by 1,000,000 shares to 3,000,000 shares. In December 2001, the Board of Directors of the Company increased the number of shares authorized for issuance under the 1999 Plan by 2,000,000 shares to 5,000,000 shares. The term for which options may be granted under the 1999 Plan expired July 12, 2009. In May 2006, the Board of Directors accelerated the vesting period for all unvested options to May 31, 2006.

2010 Stock Option and Stock Issuance Plan

On June 17, 2010 the Board of Directors approved the 2010 Stock Plan (the "2010 Plan") for officers, directors, employees and consultants of the Company. The stock issuable under the 2010 Plan shall be shares of the Company's authorized but unissued or reacquired common stock. The maximum number of shares of common stock which may be issued under the 2010 Plan is 5,000,000 shares.

The 2010 Plan is comprised of two separate equity programs, the Options Grant Program, under which eligible persons may be granted options to purchase shares of common stock, and the Stock Issuance Program, under which eligible persons may be issued shares of common stock directly, either through the immediate purchase of such shares or as a bonus for services rendered to the Company.

The 2010 Plan provides that the Board of Directors, or a committee of the Board of Directors, will administer it with full authority to determine the identity of the recipients of the options or shares and the number of options or shares. Options granted under the 2010 Plan may be either incentive stock options or non-qualified stock options. The option price shall be 100% of the fair market value of the common stock on the date of the grant (or in the case of incentive stock options granted to any individual stockholder possessing more than 10% of the total combined voting power of all voting stock of the Company, 110% of such fair market value). The term of any option may be fixed by the Board of Directors, or its authorized committee, but in no event shall it exceed five years from the date of grant. Options are exercisable upon payment in full of the exercise price, either in cash or in common stock valued at fair market value on the date of exercise of the option.

As of December 31, 2011, 3,790,000 restricted shares of common stock were granted under the 2010 Plan to non-officer employees and consultants of the Company. As of December 31, 2011, 485,000 shares have been forfeited and 198,006 were withheld for withholding taxes. In September 2010, 650,000 restricted shares of common stock were granted under the 2010 Plan to officers of the Company. In September 2011, 475,000 restricted shares of common stock were granted under the 2010 Plan to an officer, of which 100,000 vested immediately with the remainder vesting over a three year period. No options were issued under the 2010 Plan during the seven months ended December 31, 2011 and fiscal 2011 or 2010. At December 31, 2011, 766,008 shares remain available for future issuance under the 2010 Plan.

ITEM 13 - CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS AND DIRECTOR INDEPENDENCE

On February 28, 2011, David Lieberman was appointed by the Board of Directors as directors of the Company. Mr. Lieberman, a practicing attorney in the State of New York, was appointed to serve as the Vice Chairman of the Board. He is currently a senior partner at the law firm of Beckman, Lieberman & Barandes, LLP, which performs certain legal services for the Company. Fees of approximately \$166,000 were paid to the firm through the seven months ended December 31, 2011, at which time no unpaid amounts were outstanding.

William Dempsey, a director of the Company until January, 2012, was a consultant to the Company's Vaso Diagnostics subsidiary during 2011. For the seven months ended December 31, 2011, the accrued amount for consulting services was \$165,853.

Director Independence

We have adopted the NASDAQ Stock Market's standards for determining the independence of directors. Under these standards, an independent director means a person other than an executive officer or one of our employees or any other individual having a relationship which, in the opinion of the Board of Directors, would interfere with the exercise of independent judgment in carrying out the responsibilities of a director. In addition, the following persons shall not be considered independent:

- a director who is, or at any time during the past three years was, employed by us;
- a director who accepted or who has a family member who accepted any compensation from us in excess of \$100,000 during any period of twelve consecutive months within the three years preceding the determination of independence, other than the following:
 - compensation for service on the Board of Directors or any committee thereof;
 - compensation paid to a family member who is one of our employees (other than an executive officer); or
 - under a tax-qualified retirement plan, or non-discretionary compensation;
- a director who is a family member of an individual who is, or at any time during the past three years was, employed by us as an executive officer;
- a director who is, or has a family member who is, a partner in, or a controlling stockholder or an executive officer of, any organization to which we made, or from which we received, payments for property or services in the current or any of the past three fiscal years that exceed 5% of the recipient's consolidated gross revenues for that year, or \$200,000, whichever is more, other than the following:
 - payments arising solely from investments in our securities; or
 - payments under non-discretionary charitable contribution matching programs;
- a director who is, or has a family member who is, employed as an executive officer of another entity where at any time during the past three years any of our executive officers served on the compensation committee of such other entity; or
- a director who is, or has a family member who is, a current partner of our outside auditor, or was a partner or employee of our outside auditor who worked on our audit at any time during any of the past three years.

For purposes of the NASDAQ independence standards, the term "family member" means a person's spouse, parents, children and siblings, whether by blood, marriage or adoption, or anyone residing in such person's home.

The Board of Directors has assessed the independence of each non-employee director under the independence standards of the NASDAQ Stock Market set forth above, and has affirmatively determined that two of our non-employee directors (Mr. Castle and Mr. Movaseghi) are independent.

We expect each director to attend every meeting of the Board and the committees on which he serves as well as the annual meeting. In the seven months ended December 31, 2011, all directors except William Dempsey attended both the annual meeting and at least 75% of the meetings of the Board and the committees on which they served.

ITEM 14 - PRINCIPAL ACCOUNTING FEES AND SERVICES

Rothstein, Kass & Company, P.C. is our independent registered public accounting firm and performed the audits of our consolidated financial statements for the seven months ended December 31, 2011, and fiscal years 2011 and 2010. The following table sets forth all fees for the seven months ended December 31, 2011, and for the fiscal years ended May 31, 2011 and 2010:

| | Transition Period | 2011 | 2010 |
|----------------|----------------------|------------|-----------|
| Audit fees | \$ 120,149 | \$ 122,750 | \$ 75,000 |
| Tax fees | 7,448 | 15,000 | 15,000 |
| All other fees | 13,403 | - | - |
| Total | \$ 141,000 | \$ 137,750 | \$ 90,000 |

The Audit Committee has adopted a policy that requires advance approval of all audit, audit-related, tax services, and other services performed by the Company's independent auditor. Accordingly, the Audit Committee must approve the permitted service before the independent auditor is engaged to perform it. In accordance with such policies, the Audit Committee approved 100% of the services relative to the above fees.

Rothstein, Kass & Company, P.C. rendered other non-audit services related to the Company's acquisition of Fast Growth Enterprises, Ltd. during the seven months ended December 31, 2011.

PART IV

ITEM 15 – EXHIBITS AND FINANCIAL STATEMENT SCHEDULES

Financial Statements and Financial Statement Schedules

(1) See Index to Consolidated Financial Statements on page F-1 at beginning of attached financial statements.

- | | |
|-----|----------|
| (a) | Exhibits |
|-----|----------|
- (2) (a) Restated Certificate of Incorporation (2)
 (b) By-Laws (1)
- (3.1) Certificate of Designations of Preferences and Rights of Series E Convertible Preferred Stock (9)
- (4) (a) Specimen Certificate for Common Stock (1)
 (b) Specimen Certificate for Series E Convertible Preferred Stock (11)
- (10) (a) 1995 Stock Option Plan (3)
 (b) Outside Director Stock Option Plan (3)
 (c) 1997 Stock Option Plan, as amended (4)
 (d) 1999 Stock Option Plan, as amended (5)
 (e) 2004 Stock Option/Stock Issuance Plan (6)
 (f) Securities Purchase Agreement dated June 21, 2007 between Registrant and Kerns Manufacturing Corp. (7)
 (g) Form of Common Stock Purchase Warrant to dated June 21, 2007 (7)
 (h) Registration Rights Agreement dated June 21, 2007 between Registrant, Kerns Manufacturing Corp. and Living Data Technology Corporation. (7)
 (i) Purchase and Sale Agreement dated June 1, 2007 between 180 Linden Avenue Corp and 180 Linden Realty LLC. (8)
 (j) Lease Agreement dated August 15, 2007 between 180 Linden Realty LLC and Registrant (8)
 (k) Form of Stock Purchase Agreement (9)
 (l) Redacted Sales Representative Agreement between GE Healthcare Division of General Electric Company and Vaso Diagnostics, Inc. d/b/a VasoHealthcare, a subsidiary of Vasomedical, Inc. dated as of May 19, 2010 (10).
 (m) 2010 Stock Plan (11).
 (n) Consulting Agreement dated March 1, 2011 between Vasomedical, Inc. and Edgery Consultants, LLC. (12)
 (o) Employment Agreement entered into as of March 21, 2011 between Vasomedical, Inc. and Jun Ma (13).
 (p) Stock Purchase Agreement dated as of August 19, 2011 among Vasomedical, Inc., Fast Growth Enterprises Limited (FGE) and the FGE Shareholders (14)

(21) Subsidiaries of the Registrant

| Name | State of Incorporation | Percentage Owned by Company |
|---------------------------------|------------------------|-----------------------------|
| Viromedics, Inc. | Delaware | 61% |
| Vaso Diagnostics, Inc. | New York | 100% |
| Vasomedical Global Corp. | New York | 100% |
| Vasomedical Solutions, Inc. | New York | 100% |
| Fast Growth Enterprises Limited | British Virgin Islands | 100% |

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- (31) Certification Reports pursuant to Securities Exchange Act Rule 13a - 14
- (32) Certification Reports pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

-
- (1) Incorporated by reference to Registration Statement on Form S-18, No. 33-24095.
 - (2) Incorporated by reference to Registration Statement on Form S-1, No. 33-46377 (effective 7/12/94).
 - (3) Incorporated by reference to Report on Form 8-K dated January 24, 1995.
 - (4) Incorporated by reference to Report on Form 10-K for the fiscal year ended May 31, 1999
 - (5) Incorporated by reference to Report on Form 10-K for the fiscal year ended May 31, 2000.
 - (6) Incorporated by reference to Notice of Annual Meeting of Stockholders dated October 28, 2004.
 - (7) Incorporated by reference to Report on Form 8-K dated June 21, 2007.
 - (8) Incorporated by reference to Report on Form 10-KSB for the fiscal year ended May 31, 2007.
 - (9) Incorporated by reference to Report on Form 8-K dated June 21, 2010.
 - (10) Incorporated by reference to Report on Form 8-K/A dated May 29, 2010 and filed November 9, 2010.
 - (11) Incorporated by reference to Report on Form 10-K for the fiscal year ended May 31, 2010.
 - (12) Incorporated by reference to Report on Form 8-K dated March 4, 2011.
 - (13) Incorporated by reference to Report on Form 8-K dated March 21, 2011.
 - (14) Incorporated by reference to Report on Form 10-K for the fiscal year ended May 31, 2011

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, we have duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized on the 27th day of April 2012.

VASOMEDICAL, INC.

By: /s/ Jun Ma
Jun Ma
President, Chief Executive Officer,
and Director (Principal Executive Officer)

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below on April 27, 2012, by the following persons in the capacities indicated:

/s/ Jun Ma President, Chief Executive Officer
Jun Ma and Director (Principal Executive Officer)

/s/ Michael Beecher Chief Financial Officer (Principal Financial Officer)
Michael Beecher

/s/ Simon Srybnik Chairman of the Board
Simon Srybnik

/s/ David Lieberman Vice Chairman of the Board
David Lieberman

/s/ Edgar Rios Director
Edgar Rios

/ s / B e h n a m Director
Movaseghi
Behnam Movaseghi

/s/ Peter C. Castle Director
Peter C. Castle

Vasomedical, Inc. and Subsidiaries

INDEX TO CONSOLIDATED FINANCIAL STATEMENTS

For the seven months ended December 31, 2011 and for the years ended May 31, 2011 and 2010

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| Financial Statements | |
| Consolidated Balance Sheets as of December 31, 2011, May 31, 2011, and May 31, 2010 | F-3 |
| Consolidated Statements of Operations and Comprehensive Income (Loss) for the seven months ended December 31, 2011 and for the years ended May 31, 2011 and 2010 | F-4 |
| Consolidated Statements of Changes in Stockholders' Equity for the seven months ended December 31, 2011 and for the years ended May 31, 2011 and 2010 | F-5 |
| Consolidated Statements of Cash Flows for the seven months ended December 31, 2011 and for the years ended May 31, 2011 and 2010 | F-6 |
| Notes to Consolidated Financial Statements | F-7 - F-31 |

F-1

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Stockholders of
Vasomedical, Inc.

We have audited the accompanying consolidated balance sheets of Vasomedical, Inc. and Subsidiaries (collectively, the "Company") as of December 31, 2011, May 31, 2011 and 2010, and the related consolidated statements of operations and comprehensive income (loss), changes in stockholders' equity, and cash flows for the seven month period ended December 31, 2011 and for the years ended May 31, 2011 and 2010. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We did not audit the consolidated financial statements of a certain wholly-owned subsidiary, which statements reflect total assets of approximately \$1.4 million as of December 31, 2011, and total revenues of approximately \$0.8 million for the four months ended December 31, 2011. Those statements were audited by other auditors whose report has been furnished to us, and our opinion, insofar as it relates to the amounts included for the wholly-owned subsidiary, is based solely on the report of the other auditors. The opinion of the other auditors was qualified for certain assets, liabilities and disclosures of the wholly-owned subsidiary; however, in our opinion, the effects of that qualification are not material in relation to the consolidated financial statements.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, 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 and the report of the other auditors provide a reasonable basis for our opinion.

In our opinion, based on our audits and the report of the other auditors, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Vasomedical, Inc. and Subsidiaries as of December 31, 2011, May 31, 2011 and 2010, and the results of their operations and their cash flows for the seven month period ended December 31, 2011 and for the years ended May 31, 2011 and 2010 in conformity with accounting principles generally accepted in the United States of America.

/s/ Rothstein Kass

New York, New York
April 27, 2012

Vasomedical, Inc. and Subsidiaries

CONSOLIDATED BALANCE SHEETS

(in thousands, except per share data)

| | December 31, 2011 | May 31, 2011 | May 31, 2010 |
|---|----------------------|-----------------|-----------------|
| ASSETS | | | |
| CURRENT ASSETS | | | |
| Cash and cash equivalents | \$2,294 | \$8,130 | \$482 |
| Short-term investments | 110 | 110 | 69 |
| Accounts and other receivables, net of an allowance for doubtful accounts and commission adjustments of \$2,163 at December 31, 2011, \$1,297 at May 31, 2011 and \$147 at May 31, 2010 | 20,695 | 4,019 | 474 |
| Receivables due from related parties | 196 | - | - |
| Inventories, net | 2,421 | 1,786 | 2,064 |
| Financing receivables, net | 19 | 18 | - |
| Deferred commission expense | 2,053 | 2,532 | - |
| Deferred related party consulting expense - current portion | 510 | 510 | - |
| Other current assets | 202 | 267 | 91 |
| Total current assets | 28,500 | 17,372 | 3,180 |
| PROPERTY AND EQUIPMENT , net of accumulated depreciation of \$1,774 at December 31, 2011, \$1,633 at May 31, 2011 and \$1,612 at May 31, 2010 | 429 | 366 | 303 |
| GOODWILL | 3,939 | - | - |
| DEFERRED DISTRIBUTOR COSTS , net of accumulated amortization of \$589 at December 31, 2011, \$464 at May 31, 2011 and \$339 at May 31, 2010 | - | 124 | 250 |
| FINANCING RECEIVABLES , net | 16 | 27 | - |
| DEFERRED RELATED PARTY CONSULTING EXPENSE | 85 | 383 | - |
| OTHER ASSETS | 1,337 | 282 | 130 |
| | \$34,306 | \$18,554 | \$3,863 |
| LIABILITIES AND STOCKHOLDERS' EQUITY | | | |
| CURRENT LIABILITIES | | | |
| Accounts payable | \$273 | \$471 | \$266 |
| Accrued commissions | 3,889 | 1,964 | 29 |
| Accrued expenses and other liabilities | 2,531 | 694 | 327 |
| Sales tax payable | 355 | 160 | 142 |
| Income taxes payable | 278 | 10 | 6 |
| Deferred revenue - current portion | 9,484 | 10,918 | 854 |
| Deferred gain on sale-leaseback of building - current portion | 31 | 53 | 53 |
| Deferred tax liability | 112 | - | - |
| Trade payable due to related party | - | 266 | 240 |
| Notes payable due to related party | 193 | - | - |
| Total current liabilities | 17,146 | 14,536 | 1,917 |

LONG-TERM LIABILITIES

| | | | |
|---|-------|-------|-------|
| Notes payable | - | - | 1,250 |
| Deferred revenue | 5,743 | 1,004 | 173 |
| Accrued rent expense | - | 3 | 16 |
| Deferred gain on sale-leaseback of building | - | 9 | 62 |
| Other long-term liabilities | 141 | 95 | 12 |
| Total long-term liabilities | 5,884 | 1,111 | 1,513 |

COMMITMENTS AND CONTINGENCIES (NOTE R)**STOCKHOLDERS' EQUITY**

| | | | |
|---|-----------|-----------|-----------|
| Preferred stock, \$.01 par value; 1,000,000 shares authorized; nil, 299,024 and nil shares issued and outstanding at December 31, 2011, May 31, 2011 and May 31, 2010 | - | 3 | - |
| Common stock, \$.001 par value; 250,000,000 shares authorized; 153,186,295, 117,078,704 and 110,271,131 shares issued and outstanding at December 31, 2011, May 31, 2011 and May 31, 2010 | 153 | 117 | 110 |
| Additional paid-in capital | 60,188 | 55,743 | 48,959 |
| Accumulated deficit | (49,065) | (52,956) | (48,636) |
| Accumulated other comprehensive income | - | - | - |
| Total stockholders' equity | 11,276 | 2,907 | 433 |
| | \$34,306 | \$18,554 | \$3,863 |

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

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Vasomedical, Inc. and Subsidiaries

CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE INCOME (LOSS)
(in thousands, except per share data)

| | Seven months ended December 31, 2011 | Years ended May 31, 2011 | 2010 |
|--|--|--------------------------------|-------------------|
| Revenues | | | |
| Equipment sales | \$1,473 | \$3,029 | \$2,119 |
| Equipment rentals and services | 1,103 | 2,231 | 2,087 |
| Commissions | 20,913 | 11,113 | - |
| Total revenues | 23,489 | 16,373 | 4,206 |
| Cost of revenues | | | |
| Cost of sales, equipment | 814 | 1,938 | 1,163 |
| Cost of equipment rentals and services | 519 | 909 | 831 |
| Cost of commissions | 5,400 | 2,614 | - |
| Total cost of revenues | 6,733 | 5,461 | 1,994 |
| Gross profit | 16,756 | 10,912 | 2,212 |
| Operating expenses | | | |
| Selling, general and administrative | 11,243 | 14,383 | 3,773 |
| Research and development | 324 | 462 | 419 |
| Total operating expenses | 11,567 | 14,845 | 4,192 |
| Operating income (loss) | 5,189 | (3,933) | (1,980) |
| Other income (expenses) | | | |
| Interest and financing costs | (9) | (32) | (5) |
| Interest and other income, net | 177 | 28 | 80 |
| Amortization of deferred gain on sale-leaseback of building | 31 | 53 | 53 |
| Total other income, net | 199 | 49 | 128 |
| Income (loss) before income taxes | 5,388 | (3,884) | (1,852) |
| Income tax benefit (expense), net | (276) | (7) | 36 |
| Net income (loss) | 5,112 | (3,891) | (1,816) |
| Net income attributable to non-controlling interest | - | - | 76 |
| Preferred stock dividends | (1,221) | (429) | - |
| Net income (loss) applicable to common stockholders | \$3,891 | \$(4,320) | \$(1,892) |
| Other comprehensive income (loss) | | | |
| Foreign currency translation gain (loss) | - | - | - |
| Comprehensive income (loss) | \$3,891 | \$(4,320) | \$(1,892) |
| Income (loss) per common share | | | |

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| | | | | |
|-----------|--------|---------|-----------|---|
| - basic | \$0.03 | \$(0.04 |) \$(0.02 |) |
| - diluted | \$0.03 | \$(0.04 |) \$(0.02 |) |

Weighted average common shares outstanding

| | | | |
|-----------|---------|---------|---------|
| - basic | 146,549 | 111,978 | 101,776 |
| - diluted | 153,657 | 111,978 | 101,776 |

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

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Vasomedical, Inc. and Subsidiaries

CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY

(in thousands)

| | Preferred Stock Shares | Stock Amount | Common Stock Shares | Stock Amount | Additional Paid-in Capital | Accumulated Deficit | Non- controlling Interest | Accumulated Other Comprehensive Income | Total Stockholders' Equity |
|--|---------------------------|-----------------|------------------------|-----------------|----------------------------------|------------------------|---------------------------------|---|----------------------------------|
| Balance at May 31, 2009 | | \$ - | 99,843 | \$ 99 | \$ 48,282 | \$ (46,744) | \$ (76) | \$ - | \$ 1,561 |
| Common stock issued for inventory purchase | | | 7,824 | 8 | 462 | | | | 470 |
| Common stock issued to Director for fiscal year 2009 compensation and meeting fees | | | 1,937 | 2 | 149 | | | | 151 |
| Share-based compensation | | | 667 | 1 | 39 | | | | 40 |
| Options granted as compensation to one officer and one director | | | | | 27 | | | | 27 |
| Net income (loss) | | | | | | (1,892) | 76 | | (1,816) |
| Balance at May 31 , 2010 | - | \$ - | 110,271 | \$ 110 | \$ 48,959 | \$ (48,636) | \$ - | \$ - | \$ 433 |
| Common stock issued to directors for fiscal year 2011 compensation and meeting fees | | | 750 | 1 | 177 | | | | 178 |
| Share-based compensation | | | 995 | 1 | 267 | | | | 268 |
| Shares granted for consulting agreements | | | 3,116 | 3 | 1,086 | | | | 1,089 |
| Shares issued on exercise of warrant | | | 384 | | - | | | | - |
| Preferred shares sold (including converted notes payable) | 308 | 3 | | | 4,930 | | | | 4,933 |
| Preferred shares issued as dividends | 6 | | | | 101 | | | | 101 |
| Beneficial conversion | | | | | 225 | | | | 225 |

| | | | | | | | | | |
|--|--------|------|---------|--------|-----------|--------------|------|------|-----------|
| feature of Preferred shares | | | | | | | | | |
| Preferred share dividends | | | | | | (429) | | | (429) |
| Conversion of preferred shares | (16) | | 1,563 | 2 | | (2) | | | - |
| Net loss | | | | | | (3,891) | | | (3,891) |
| Balance at May 31, 2011 | 298 | \$ 3 | 117,079 | \$ 117 | \$ 55,743 | \$ (52,956) | \$ - | \$ - | \$ 2,907 |
| Common stock issued to | | | | | | | | | |
| Director | | | 50 | | | 23 | | | 23 |
| Share-based compensation | | | 894 | 1 | | 184 | | | 185 |
| Shares not issued for employee tax liability | | | | | | (80) | | | (80) |
| Shares granted for consulting agreements | | | 208 | | | 47 | | | 47 |
| Common shares, warrants and contingent shares issued for acquisition | | | 5,000 | 5 | | 2,974 | | | 2,979 |
| Beneficial conversion feature of Preferred shares | | | | | | 1,201 | | | 1,201 |
| Preferred shares issued as dividends | 7 | | | | | 123 | | | 123 |
| Preferred share dividends | | | | | | (1,221) | | | (1,221) |
| Conversion of preferred shares | (305) | (3) | 29,956 | 30 | | (27) | | | - |
| Foreign currency translation gain (loss) | | | | | | | | - | - |
| Net income | | | | | | 5,112 | | | 5,112 |
| Balance at December 31, 2011 | - | \$ - | 153,187 | \$ 153 | \$ 60,188 | \$ (49,065) | \$ - | \$ - | \$ 11,276 |

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

Vasomedical, Inc. and Subsidiaries

CONSOLIDATED STATEMENTS OF CASH FLOWS

(in thousands)

| | Seven Months ended December 31, 2011 | Years ended May 31, 2011 | May 31, 2010 |
|---|--|-----------------------------|-----------------|
| Cash flows from operating activities | | | |
| Net income (loss) | \$ 5,112 | \$ (3,891) | \$ (1,816) |
| Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities | | | |
| Depreciation and amortization of property and equipment | 101 | 144 | 123 |
| Amortization of deferred gain on sale-leaseback of building | (31) | (53) | (53) |
| Losses (gains) on disposal of fixed assets | (5) | - | - |
| Provision for doubtful accounts and commission adjustments | 866 | 1,150 | 52 |
| Amortization of deferred distributor costs | 124 | 126 | 126 |
| Share-based compensation | 208 | 446 | 218 |
| Amortization of deferred consulting expense | 370 | 154 | - |
| Changes in operating assets and liabilities: | | | |
| Accounts and other receivables | (16,986) | (4,696) | 167 |
| Receivables due from related parties | (196) | - | - |
| Inventories, net | (186) | 248 | (288) |
| Finance receivables | 11 | (46) | - |
| Deferred commission expense | 479 | (2,533) | - |
| Other current assets | 41 | (133) | 51 |
| Other assets | (1,074) | (194) | - |
| Accounts payable | (657) | 205 | 179 |
| Accrued commissions | 1,925 | 1,935 | (1) |
| Accrued expenses and other liabilities | 1,398 | 264 | (46) |
| Sales tax payable | 98 | 18 | (2) |
| Income taxes payable | 221 | 4 | (20) |
| Deferred revenue | 3,305 | 10,895 | (260) |
| Accrued rent expense | (5) | (13) | 2 |
| Deferred tax liability | - | - | - |
| Trade payable due to related party | (268) | 26 | (20) |
| Other long-term liabilities | 46 | 83 | - |
| Net cash provided by (used in) operating activities | (5,103) | 4,139 | (1,588) |
| Cash flows from investing activities | | | |
| Purchases of property and equipment | (80) | (135) | (26) |

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| | | | |
|---|-------------|-----------|--------|
| Purchases of short-term investments | - | (40) | (69) |
| Redemption of short-term investments | - | - | 371 |
| Acquisition of Fast Growth Enterprises | (1,000) | - | - |
| Cash acquired through purchase of Fast Growth Enterprises | 442 | - | - |
| Net cash provided by (used in) investing activities | (638) | (175) | 276 |
| Cash flows from financing activities | | | |
| Issuance of note payable | - | 250 | 1,250 |
| Repayment of note payable | - | (250) | - |
| Repayment of notes payable due to related party | (95) | - | - |
| Proceeds from preferred stock | - | 3,684 | - |
| Net cash (used in) provided by financing activities | (95) | 3,684 | 1,250 |
| Effect of exchange rate differences on cash | - | - | - |
| NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS | | | |
| | (5,836) | 7,648 | (62) |
| Cash and cash equivalents - beginning of period | 8,130 | 482 | 544 |
| Cash and cash equivalents - end of period | \$ 2,294 | \$ 8,130 | \$ 482 |
| SUPPLEMENTAL DISCLOSURE OF CASH INFORMATION | | | |
| Interest paid | \$ 11 | 8 | - |
| Income taxes paid | \$ 22 | 8 | 6 |
| SUPPLEMENTAL SCHEDULE OF NON-CASH INVESTING AND FINANCING ACTIVITIES | | | |
| Inventories transferred to property and equipment, | | | |
| attributable to operating leases, net | \$ 27 | \$ 30 | \$ 173 |
| Conversion of notes payable to preferred stock | \$ - | \$ 1,250 | \$ - |
| Accrued preferred stock dividends | \$ (1,221) | \$ (429) | \$ - |
| Common shares, warrants and contingent shares issued for acquisition | \$ 2,979 | \$ - | \$ - |
| Fair value of assets acquired | \$ 4,731 | \$ - | \$ - |
| Liabilities assumed through acquisition | \$ (1,194) | \$ - | \$ - |
| Trade Payable due to related party paid on common stock | \$ - | \$ - | \$ 469 |
| Issuance of preferred stock in satisfaction of accrued dividend | \$ 123 | \$ 101 | \$ - |
| Conversion of preferred stock to common stock | \$ 30 | \$ 2 | \$ - |
| Common shares issued for consulting agreements | \$ - | \$ 1,070 | \$ - |

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

Vasomedical, Inc. and Subsidiaries

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2011, May 31, 2011 and 2010

NOTE A – DESCRIPTION OF BUSINESS, LIQUIDITY AND CHANGE IN FISCAL YEAR END

Vasomedical, Inc. was incorporated in Delaware in July 1987. Unless the context requires otherwise, all references to “we”, “our”, “us”, “Company”, “registrant”, “Vasomedical” or “management” refer to Vasomedical, Inc. and its subsidiaries. Since 1995, we have been engaged in designing, manufacturing, marketing and supporting EECP® Enhanced External Counterpulsation systems, based on our unique proprietary technology, to physicians and hospitals throughout the United States and in select international markets.

In 2010, the Company, through its wholly-owned subsidiary Vaso Diagnostics d/b/a VasoHealthcare, organized a group of medical device sales professionals and entered into the sales representation business as the exclusive representative for the sale of select General Electric Company (GE) diagnostic imaging equipment to specific market segments in the 48 contiguous states of the United States and the District of Columbia.

In September 2011, the Company acquired Fast Growth Enterprises Limited (FGE), a British Virgin Islands company, which, through its subsidiaries, owns and controls two Chinese operating companies - Life Enhancement Technology Ltd. and Biox Instruments Co. Ltd., respectively - to expand its technical and manufacturing capabilities and to enhance its distribution network, technology, and product portfolio. Also in September 2011, the Company restructured to further align its business management structure and long-term growth strategy, and now operates through three wholly-owned subsidiaries. Vaso Diagnostics d/b/a VasoHealthcare continues as the operating subsidiary for the sales representation of GE diagnostic imaging products; Vasomedical Global Corp. operates the Company’s newly-acquired Chinese companies; and Vasomedical Solutions, Inc. was formed to manage and coordinate our EECP® therapy business as well as other medical equipment operations.

We have achieved profitability through the operations of the VasoHealthcare business. The Company will seek to achieve greater profitability through our recent accretive acquisition of the two Chinese medical device companies and by expanding our U.S. market product portfolio. In addition, the Company plans to actively pursue other accretive acquisitions in the international market and is in preliminary discussions to secure a credit facility for up to \$25 million to be utilized for this purpose.

Based on our current operations through December 31, 2011, we believe internally generated funds from our Equipment and Sales Representation segments will be sufficient for the Company to continue operations through at least January 1, 2013.

On June 15, 2011, the Board of Directors approved a change of the Company’s fiscal year end from May 31st to December 31st. As a result of this change, the Company is filing a Transition Report on Form 10-K for the seven-month transition period ended December 31, 2011. References to any of our fiscal years means the fiscal year ending May 31, 2011 or 2010. Financial information in these notes with respect to the seven months ended December 31, 2010 is unaudited.

NOTE B - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A summary of the significant accounting policies consistently applied in the preparation of the consolidated financial statements are as follows:

Principles of Consolidation

The consolidated financial statements include the accounts of the Company, its wholly-owned subsidiaries, its inactive majority-owned subsidiary, and variable interest entities where the Company is the primary beneficiary. Significant intercompany accounts and transactions have been eliminated.

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Vasomedical, Inc. and Subsidiaries

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2011, May 31, 2011 and 2010

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America (“U.S. GAAP”) requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying notes. Significant estimates and assumptions relate to estimates of collectibility of accounts receivable, the realizability of deferred tax assets, stock-based compensation and the adequacy of inventory and warranty reserves. Additionally, significant estimates and assumptions impact the Company's accounting relative to its business combination. Actual results could differ from those estimates.

Revenue Recognition

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

In most cases, revenue from domestic EECPC® system sales is generated from multiple-element arrangements that require judgment in the areas of customer acceptance, collectability, the separability of units of accounting, and the fair value of individual elements. We follow the FASB Accounting Standards Codification (“ASC”) Topic 605 “Revenue Recognition” (“ASC 605”) which outlines a framework for recognizing revenue from multi-deliverable arrangements. The principles and guidance outlined in ASC 605 provide a framework to determine (a) how the arrangement consideration should be measured (b) whether the arrangement should be divided into separate units of accounting, and (c) how the arrangement consideration should be allocated among the separate units of accounting. We determined that the domestic sale of our EECPC® systems includes a combination of three elements that qualify as separate units of accounting:

- EECPC® equipment sale;
- provision of in-service and training support consisting of equipment set-up and training provided at the customer's facilities; and
- a service arrangement (usually one year), consisting of: service by factory-trained service representatives, material and labor costs, emergency and remedial service visits, software upgrades, technical phone support and preferred response times.

Each of these elements represent individual units of accounting as the delivered item has value to a customer on a stand-alone basis, objective and reliable evidence of fair value exists for undelivered items, and arrangements normally do not contain a general right of return relative to the delivered item. We determine fair value based on the price of the deliverable when it is sold separately, or based on third-party evidence, or based on estimated selling price. Assuming all other criteria for revenue recognition have been met, we recognize revenue for:

- EECPC® equipment sales, when delivery and acceptance occurs based on delivery and acceptance documentation received from independent shipping companies or customers;
 - in-service and training, following documented completion of the training; and
 - service arrangement, ratably over the service period, which is generally one year.

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

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Vasomedical, Inc. and Subsidiaries

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2011, May 31, 2011 and 2010

The Company also recognizes revenue generated from servicing EEC[®] systems that are no longer covered by the service arrangement, or by providing sites with additional training, in the period that these services are provided. Revenue related to future commitments under separately priced extended service agreements on our EEC[®] system are deferred and recognized ratably over the service period, generally ranging from one year to four years. Costs associated with the provision of service and maintenance, including salaries, benefits, travel and spare parts, and equipment, are recognized in cost of sales as incurred. Amounts billed in excess of revenue recognized are included as deferred revenue in the Consolidated Balance Sheets.

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

Revenue and Expense Recognition for VasoHealthcare

The Company recognizes commission revenue in its Sales Representation segment (see Note C) when persuasive evidence of an arrangement exists, service has been rendered, the price is fixed or determinable and collectability is reasonably assured. These conditions are deemed to be met when the underlying equipment has been accepted at the customer site in accordance with the specific terms of the sales agreement. Consequently, amounts billable under the agreement with GE Healthcare in advance of the customer acceptance of the equipment are recorded as accounts receivable and deferred revenue in the Consolidated Balance Sheets. Similarly, commissions payable to our sales force related to such billings are recorded as deferred commission expense when the associated deferred revenue is recorded. Commission expense is recognized when the corresponding commission revenue is recognized.

Shipping and Handling Costs

All shipping and handling expenses are charged to cost of sales. Amounts billed to customers related to shipping and handling costs are included as a component of sales.

Research and Development

Research and development costs attributable to development are expensed as incurred. Included in research and development costs is amortization expense related to the capitalized cost of EEC[®] systems under loan for clinical trials.

Share-Based Compensation

The Company complies with ASC Topic 718 “Compensation – Stock Compensation” (“ASC 718”), which requires all companies to recognize the cost of services received in exchange for equity instruments, to be recognized in the financial statements based on their fair values.

During fiscal 2011, the Company’s Board of Directors granted, under the 2010 Stock Plan (see Note P), 4,440,000 restricted shares of common stock valued at \$876,000 to employees and consultants. 355,000 shares valued at \$72,000 vested immediately and the remainder vest over three years. During fiscal 2011, 4,116,279 shares of common stock valued at \$1,325,000 were granted to outside directors and consultants, of which 250,000 shares valued at \$78,000 will vest over one year. During the fiscal year ended May 31, 2010, the Company’s Board of Directors

granted 666,668 shares of common stock to two officers of the Company in lieu of a portion of their calendar year 2010 salaries, which was amortized over the remainder of calendar year 2010.

During fiscal 2011, the Company's Board of Directors did not grant any non-qualified stock options. During fiscal year 2010 the Company's Board of Directors granted options for 250,000 shares of common stock to one officer and options for 200,000 shares to one director of the Company, pursuant to the 2004 Stock Option Plan. These options have an exercise price of \$0.08 per share and expire five years from date of grant.

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Vasomedical, Inc. and Subsidiaries

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2011, May 31, 2011 and 2010

Share-based compensation expense recognized for the seven months ended December 31, 2011 and fiscal years ended May 31, 2011 and 2010 was \$208,000, \$446,000, and \$218,000, respectively. Expense for other share-based arrangements was \$370,000 and \$154,000 for the seven months ended December 31, 2011 and for the year ended May 31, 2011, respectively. Unrecognized expense related to existing share-based arrangements is approximately \$0.9 million at December 31, 2011 and will be recognized ratably through July 2013.

Vasomedical accounts for share-based compensation in accordance with fair value recognition provisions, under which the Company uses the Black-Scholes Merton option pricing model which requires the input of subjective assumptions. These assumptions include estimating the length of time employees will retain their stock options before exercising them ("expected term"), the estimated volatility of the Company's common stock price over the expected term and the number of options that will ultimately not complete their vesting requirements. The Company estimates the expected term and forfeitures based on the terms set forth in the option agreements and no assumption that any options will not complete their vesting period, which approximates actual historical behavior, and it estimates volatility of the Company's stock based on the Company's historical stock price performance over the past five years. Changes in the subjective assumptions could materially affect the estimate of fair value of share-based compensation; however management believes changes in certain assumptions that could be reasonably possible in the near term, would not have a material effect on the expense recognized for the seven months ended December 31, 2011.

The fair value of the Company's stock options was estimated using the following weighted-average assumptions for options granted during the year ended May 31, 2010:

| | |
|---------------------------------|---------|
| Expected dividend yield | 0.00% |
| Average risk free interest rate | 2.24% |
| Expected life | 5 years |
| Expected volatility | 102.31% |

Cash and Cash Equivalents

Cash and cash equivalents represent cash and short-term, highly liquid investments either in certificates of deposit, treasury bills, money market funds, or investment grade commercial paper issued by major corporations and financial institutions that generally have maturities of three months or less from the date of acquisition. Dividend and interest income are recognized when earned. The cost of securities sold is calculated using the specific identification method.

Short-Term Investments

The Company's short-term investments consist of certificates of deposit with original maturities greater than three months. They are bought and held principally for the purpose of selling them in the near-term and are classified as trading securities. Trading securities are recorded at fair value on the consolidated balance sheets in current assets, with the change in fair value during the years included in earnings.

Accounts Receivable, net

The Company's accounts receivable are due from customers engaged in the provision of medical services and from GEHC. Credit is extended based on evaluation of a customer's financial condition and, generally, collateral is not

required. Accounts receivable are generally due 30 to 90 days from shipment and are stated at amounts due from customers net of allowances for doubtful accounts, returns, term discounts and other allowances. Accounts that remain outstanding longer than the contractual payment terms are considered past due. Estimates are used in determining the allowance for doubtful accounts based on the Company's historical collections experience, current trends, credit policy and a percentage of its accounts receivable by aging category. In determining these percentages, the Company reviews historical write-offs of their receivables. The Company also looks at the credit quality of their customer base as well as changes in their credit policies. The Company continuously monitors collections and payments from our customers, and writes off receivables when all efforts at collection have been exhausted. While credit losses have historically been within expectations and the provisions established, the Company cannot guarantee that it will continue to experience the same credit loss rates that they have in the past.

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Vasomedical, Inc. and Subsidiaries

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2011, May 31, 2011 and 2010

The changes in the Company's allowance for doubtful accounts and commission adjustments are as follows:

(in thousands)

| | December 31, 2011 | May 31, 2011 | May 31, 2010 |
|---|----------------------|-----------------|-----------------|
| Beginning Balance | \$1,297 | \$147 | \$95 |
| Provision for losses on accounts receivable | 55 | (1) | 71 |
| Direct write-offs, net of recoveries | - | (58) | (19) |
| Commission adjustments | 811 | 1,209 | - |
| Ending Balance | \$2,163 | \$1,297 | \$147 |

Concentrations of Credit Risk

We market our equipment principally to hospitals and physician private practices. We perform credit evaluations of our customers' financial condition and, as a consequence, believe that our receivable credit risk exposure is limited. For the seven months ended December 31, 2011 and the years ended May 31, 2011 and 2010, no customer in our Equipment segment accounted for 10% or more of revenues or accounts receivable. In our Sales Representation segment, 100% of our revenues and accounts receivable are with GE; however, we believe this risk is acceptable based on GE's financial position.

The Company maintains cash balances in certain U.S. financial institutions, which, at times, may exceed the Federal Depository Insurance Corporation ("FDIC") coverage of \$250,000. The Company has not experienced any losses on these accounts and believes it is not subject to any significant credit risk on these accounts. In addition, the FDIC does not insure the Company's foreign cash, which aggregated approximately \$493,000 (including approximately \$186,000 maintained in the names of officers of BIOX at December 31, 2011, which accounts are properly recorded in the books and records of the Company).

Our revenues were derived from the following geographic areas:

(in thousands)

| | For the seven months ended December 31, 2011 | For the years ended May 31, 2011 | May 31, 2010 |
|--------------------------|---|--|-----------------|
| Domestic (United States) | \$22,391 | \$14,414 | \$2,954 |
| Non-domestic (foreign) | 1,098 | 1,959 | 1,252 |
| | \$23,489 | \$16,373 | \$4,206 |

Inventories, net

The Company values inventory at the lower of cost or estimated market, with cost being determined on a first-in, first-out basis. The Company often places EECPC® systems at various field locations for demonstration, training, evaluation, and other similar purposes at no charge. The cost of these EECPC® systems is transferred to property and equipment and is amortized over two to five years. The Company records the cost of refurbished components of

EECP® systems and critical components at cost plus the cost of refurbishment. The Company regularly reviews inventory quantities on hand, particularly raw materials and components, and records a provision for excess and obsolete inventory based primarily on existing and anticipated design and engineering changes to its products as well as forecasts of future product demand.

We comply with the provisions of ASC Topic 330 “Inventory”. The statement clarifies that abnormal amounts of idle facility expense, freight, handling costs, and wasted materials (spoilage) should be recognized as current-period charges and requires the allocation of fixed production overhead to inventory based on the normal capacity of the production facilities.

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Vasomedical, Inc. and Subsidiaries

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2011, May 31, 2011 and 2010

Property and Equipment

Property and equipment are stated at cost less accumulated depreciation and amortization. Major improvements are capitalized and minor replacements, maintenance and repairs are charged to expense as incurred. Upon retirement or disposal of assets, the cost and related accumulated depreciation are removed from the consolidated balance sheets. Depreciation is expensed over the estimated useful lives of the assets, which range from two to twenty years, on a straight-line basis. Accelerated methods of depreciation are used for tax purposes. We amortize leasehold improvements over the useful life of the related leasehold improvement or the life of the related lease, whichever is less. (See Note H)

Goodwill

Goodwill represents the excess of cost over the fair value of net assets of businesses acquired. The Company accounts for goodwill under the guidance of the ASC Topic 350 – “Intangibles: Goodwill and Other”. Goodwill acquired in a purchase business combination and determined to have an indefinite useful life is not amortized, but instead tested for impairment, at least annually, in accordance with this guidance.

Deferred Revenue

We record revenue on extended service contracts ratably over the term of the related service contracts. Under the provisions of ASC 605, we began to defer revenue related to EECP® system sales for the fair value of installation and in-service training to the period when the services are rendered and for service obligations ratably over the service period, which is generally one year. (See Note J)

Amounts billable under the agreement with GE Healthcare in advance of customer acceptance of the equipment are recorded initially as deferred revenue, and commission revenue is subsequently recognized as customer acceptance of such equipment is reported to us by GEHC.

Warranty Costs

Equipment sold is generally covered by a warranty period of one year. In accordance with ASC Topic 450 “Loss Contingencies”, we accrue a warranty reserve for estimated costs of providing a parts only warranty when the equipment sale is recognized.

The factors affecting our warranty liability include the number of units sold and the historical and anticipated rates of claims and costs per claim. (See Note L)

Income Taxes

Deferred income taxes are recognized for temporary differences between financial statement and income tax bases of assets and liabilities and loss carryforwards for which income tax benefits are expected to be realized in future years. A valuation allowance is established, when necessary, to reduce deferred tax assets to the amount expected to be realized. In estimating future tax consequences, we generally consider all expected future events other than an enactment of changes in the tax laws or rates. Deferred tax assets are continually evaluated for realizability. To the extent our judgment regarding the realization of the deferred tax assets changes, an adjustment to the allowance is recorded, with an offsetting increase or decrease, as appropriate, in income tax expense. Such adjustments are

recorded in the period in which our estimate as to the realizability of the assets changed that it is “more likely than not” that all of the deferred tax assets will be realized. The “realizability” standard is subjective and is based upon our estimate of a greater than 50% probability that the deferred tax asset can be realized.

Deferred tax assets and liabilities are classified as current or non-current based on the classification of the related asset or liability for financial reporting. A deferred tax asset or liability that is not related to an asset or liability for financial reporting, including deferred tax assets related to carryforwards, are classified according to the expected reversal date of the temporary difference.

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Vasomedical, Inc. and Subsidiaries

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2011, May 31, 2011 and 2010

The Company also complies with the provisions of ASC Topic 740 “Income Taxes”, which prescribes a recognition threshold and a measurement attribute for the financial statement recognition and measurement of tax positions taken or expected to be taken in a tax return. For those benefits to be recognized, a tax position must be more-likely-than-not to be sustained upon examination by the relevant taxing authority based on the technical merits. The tax benefit recognized is measured as the largest amount of benefit that has a greater than fifty percent likelihood of being realized upon ultimate settlement with the relevant taxing authority. Derecognition of a tax benefit previously recognized results in the Company recording a tax liability that reduces ending retained earnings. Based on its analysis, except for certain liabilities assumed in the FGE acquisition, the Company has determined that it has not incurred any liability for unrecognized tax benefits as of December 31, 2011, May 31, 2011 and May 31, 2010. The Company recognizes accrued interest and penalties related to unrecognized tax benefits as income tax expense. No amounts were accrued for the payment of interest and penalties at December 31, 2011, May 31, 2011 and May 31, 2010. Generally, the Company is no longer subject to income tax examinations by major domestic taxing authorities for years before 2008. According to the China tax regulatory framework, there is no statute of limitations on examination of tax filings by tax authorities. However, the general practice is going back five years. Management is currently unaware of any issues under review that could result in significant payments, accruals or material deviations from its position.

Foreign Currency Translation Gain (Loss) and Comprehensive Income (Loss)

In countries in which the Company operates, and the functional currency is other than the U.S. dollar, assets and liabilities are translated using published exchange rates in effect at the consolidated balance sheet date. Revenues and expenses and cash flows are translated using an approximate weighted average exchange rate for the period. Resulting translation adjustments are recorded as a component of accumulated other comprehensive income on the consolidated balance sheet. For the seven months ended December 31, 2011, comprehensive income (loss) includes a loss of \$108, which is entirely from foreign currency translation.

Fair Value of Financial Instruments

The Company complies with the provisions of ASC 820 “Fair Value Measurements and Disclosures” (“ASC 820”). Under ASC 820, fair value is defined as the price that would be received to sell an asset or paid to transfer a liability (i.e., the “exit price”) in an orderly transaction between market participants at the measurement date.

In determining fair value, the Company uses various valuation approaches. ASC 820 establishes a fair value hierarchy for inputs used in measuring fair value that maximizes the use of observable inputs and minimizes the use of unobservable inputs by requiring that the most observable inputs be used when available. Observable inputs are those that market participants would use in pricing the asset or liability based on market data obtained from sources independent of the Company. Unobservable inputs reflect the Company’s assumptions about the inputs market participants would use in pricing the asset or liability developed based on the best information available in the circumstances. The fair value hierarchy is categorized into three levels based on the inputs as follows:

Level 1 - Valuations based on unadjusted quoted prices in active markets for identical assets or liabilities that the Company has the ability to access. Valuation adjustments and block discounts are not applied to Level 1 securities. Since valuations are based on quoted prices that are readily and regularly available in an active market, valuation of these securities does not entail a significant degree of judgment.

Level 2 - Valuations based on quoted prices in markets that are not active or for which all significant inputs are observable, either directly or indirectly.

Level 3 - Valuations based on inputs that are unobservable and significant to the overall fair value measurement.

Valuation Techniques

The Company values investments in securities and securities sold short that are freely tradable and are listed on a national securities exchange or reported on the NASDAQ national market at their last sales price as of the last business day of the fiscal year.

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Vasomedical, Inc. and Subsidiaries

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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The carrying amounts of cash and cash equivalents, accounts receivable and accounts payable approximate fair value due to the short-term maturities of the instruments.

Net Income (Loss) Per Common Share

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

Diluted earnings per share were computed based on the weighted average number of shares outstanding plus all potentially dilutive common shares. A reconciliation of basic to diluted shares used in the earnings per share calculation is as follows:

(in thousands)

| | Seven months ended December 31, 2011 | Years ended May 31, 2011 | 2010 |
|--|---|-----------------------------|---------|
| Basic weighted average shares outstanding | 146,549 | 111,978 | 101,776 |
| Dilutive effect of share-based compensation and warrants | 5,124 | - | - |
| Dilutive effect of contingently issuable shares | 1,984 | - | - |
| Diluted weighted average shares outstanding | 153,657 | 111,978 | 101,776 |

The following table represents common stock equivalents that were excluded from the computation of diluted earnings per share for the seven months ended December 31, 2011 and for the fiscal years ended May 31, 2011 and 2010, because the effect of their inclusion would be anti-dilutive.

(in thousands)

| | December 31, 2011 | May 31, 2011 | May 31, 2010 |
|-----------------------------|----------------------|-----------------|-----------------|
| Stock options | 260 | 1,864 | 2,964 |
| Warrants | 1,500 | 4,286 | 6,969 |
| Convertible preferred stock | - | 30,545 | - |
| Common stock grants | 375 | 3,912 | - |
| | 2,135 | 40,607 | 9,933 |

Reclassifications

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

Recently Issued Accounting Pronouncements

The Company continually assesses any new accounting pronouncements to determine their applicability to the Company. Where it is determined that a new accounting pronouncement affects the Company's financial reporting, the Company undertakes a study to determine the consequence of the change to its financial statements and assures that there are proper controls in place to ascertain that the Company's consolidated financial statements properly reflect the change. New pronouncements assessed by the Company recently are discussed below:

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Vasomedical, Inc. and Subsidiaries

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2011, May 31, 2011 and 2010

Adoption of New Standards

Other Comprehensive Income: Presentation of Comprehensive Income

In June 2011, new guidance was issued that amends the current comprehensive income guidance. The new guidance allows the option to present the total of comprehensive income, the components of net income, and the components of other comprehensive income either in a single or continuous statement of comprehensive income or in two separate but consecutive statements. The amendments in this update do not change the items that must be reported in other comprehensive income or when an item of other comprehensive income must be reclassified to net income. The new guidance is to be applied retrospectively and is effective for fiscal years, and interim periods, beginning after December 15, 2011, with early adoption permitted. The Company has elected early adoption of this guidance and does not expect that it will have a material impact on the Company's consolidated financial statements.

Intangibles—Goodwill and Other: Testing Goodwill for Impairment

In September 2011, an accounting standard update regarding testing of goodwill for impairment was issued. This standard update gives companies the option to perform a qualitative assessment to first assess whether the fair value of a reporting unit is less than its carrying amount. If an entity determines it is not more likely than not that the fair value of the reporting unit is less than its carrying amount, then performing the two-step impairment test is unnecessary. The new guidance is to be applied prospectively effective for annual and interim goodwill impairment tests beginning after December 15, 2011, with early adoption permitted. The Company has elected early adoption of this guidance and does not expect that it will have a material impact on the Company's consolidated financial statements.

NOTE C – SEGMENT REPORTING

The Company views its business in two segments – the Equipment segment and the Sales Representation segment. The Equipment segment is engaged in designing, manufacturing, marketing and supporting EECP® enhanced external counterpulsation systems and other medical devices both domestically and internationally. The Sales Representation segment operates through the VasoHealthcare subsidiary and is engaged solely in the execution of the Company's responsibilities under our agreement with GEHC. The Company evaluates segment performance based on operating income. Administrative functions such as finance, human resources, and information technology are centralized and related expenses allocated to each segment. There are no intersegment revenues. Summary financial information for the segments is set forth below:

Vasomedical, Inc. and Subsidiaries

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2011, May 31, 2011 and 2010

(in thousands)

| As of or for the seven months ended December 31, 2011 | | | | |
|---|----------------------|------------------------------------|-----------|--------------|
| | Equipment Segment | Sales Representation Segment | Corporate | Consolidated |
| Revenues from external customers | \$ 2,576 | \$ 20,913 | \$ - | \$ 23,489 |
| Operating income/(loss) | \$ (1,603) | \$ 7,417 | \$ (625) | \$ 5,189 |
| Total assets | \$ 9,178 | \$ 22,877 | \$ 2,251 | \$ 34,306 |
| Accounts and other receivables, net | \$ 901 | \$ 19,794 | \$ - | \$ 20,695 |
| Deferred commission expense | \$ - | \$ 3,185 | \$ - | \$ 3,185 |
| As of or for the year ended May 31, 2011 | | | | |
| | Equipment Segment | Sales Representation Segment | Corporate | Consolidated |
| Revenues from external customers | \$ 5,260 | \$ 11,113 | \$ - | \$ 16,373 |
| Operating income/(loss) | \$ (530) | \$ (2,962) | \$ (441) | \$ (3,933) |
| Total assets | \$ 4,504 | \$ 5,920 | \$ 8,130 | \$ 18,554 |
| Accounts and other receivables, net | \$ 932 | \$ 3,087 | \$ - | \$ 4,019 |
| Deferred commission expense | \$ - | \$ 2,723 | \$ - | \$ 2,723 |
| As of or for the year ended May 31, 2010 | | | | |
| | Equipment Segment | Sales Representation Segment | Corporate | Consolidated |
| Revenues from external customers | \$ 4,206 | \$ - | \$ - | \$ 4,206 |
| Operating income/(loss) | \$ (429) | \$ (1,057) | \$ (494) | \$ (1,980) |
| Total assets | \$ 3,338 | \$ 44 | \$ 481 | \$ 3,863 |
| Accounts and other receivables, net | \$ 474 | \$ - | \$ - | \$ 474 |
| Deferred commission expense | \$ - | \$ - | \$ - | \$ - |

For the seven months ended December 31, 2011 and the year ended May 31, 2011, GE Healthcare accounted for 89% and 68% of revenue, respectively. Also, GE Healthcare accounted for \$19.7 million, or 95%, and \$3.0 million, or 74%, of accounts and other receivables at December 31, 2011 and May 31, 2011, respectively.

NOTE D – FAIR VALUE MEASUREMENTS

The Company's assets recorded at fair value have been categorized based upon a fair value hierarchy in accordance with ASC 820.

The following table presents information about the Company's assets and liabilities measured at fair value as of December 31, 2011:

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Vasomedical, Inc. and Subsidiaries

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(in thousands)

| | Quoted Prices in Active Markets for Identical Assets (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) | Balance as of December 31, 2011 |
|---|--|---|--|---|
| Assets | | | | |
| Cash equivalents invested in money market funds (included in cash and cash equivalents) | \$1,313 | \$- | \$ - | \$1,313 |
| Investment in certificates of deposit (included in short-term investments) | 110 | | | 110 |
| | \$1,423 | \$- | \$ - | \$1,423 |

The following table presents information about the Company's assets and liabilities measured at fair value as of May 31, 2011:

(in thousands)

| | Quoted Prices in Active Markets for Identical Assets (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) | Balance as of December 31, 2011 |
|---|--|---|--|---|
| Assets | | | | |
| Cash equivalents invested in money market funds (included in cash and cash equivalents) | \$7,030 | \$- | \$ - | \$7,030 |
| Investment in certificates of deposit (included in short-term investments) | 110 | - | - | 110 |
| | \$7,140 | \$- | \$ - | \$7,140 |

The following table presents information about the Company's assets and liabilities measured at fair value as of May 31, 2010:

(in thousands)

| | Quoted Prices in Active Markets for Identical Assets (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) | Balance as of December 31, 2010 |
|--|--|---|--|---|
|--|--|---|--|---|

Assets

Cash equivalents invested in money market funds (included in

cash and cash equivalents) \$21 \$- \$ - \$21

Investment in certificates of deposit (included in short-term investments)

69 - - 69

\$90 \$- \$ - \$90

The fair values of the Company's cash equivalents invested in money market funds are determined through market, observable and corroborated sources.

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Vasomedical, Inc. and Subsidiaries

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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NOTE E – ACCOUNTS AND OTHER RECEIVABLES

The following table presents information regarding the Company's accounts and other receivables as of December 31, 2011; May 31, 2011 and May 31, 2010:

(in thousands)

| | December 31, 2011 | May 31, 2011 | May 31, 2010 |
|---|----------------------|-----------------|-----------------|
| Trade receivables | \$22,737 | \$5,195 | \$588 |
| Due from employees | 121 | 121 | 33 |
| Allowance for doubtful accounts and commission adjustments | (2,163) | (1,297) | (147) |
| | \$20,695 | \$4,019 | \$474 |

Trade receivables include amounts due for shipped products and services rendered. Amounts currently due under the GEHC Agreement are subject to adjustment in subsequent periods should the underlying sales order amount, upon which the receivable is based, change.

Allowance for doubtful accounts and commission adjustments include estimated losses resulting from the inability of our customers to make required payments, and adjustments arising from subsequent changes in sales order amounts that may reduce the amount the Company will ultimately receive under the GEHC Agreement. Due from employees primarily reflects commission advances made to sales personnel.

NOTE F – INVENTORIES, NET

Inventories, net of reserves consisted of the following:

(in thousands)

| | December 31, 2011 | May 31, 2011 | May 31, 2010 |
|-----------------|----------------------|-----------------|-----------------|
| Raw materials | \$842 | \$514 | \$599 |
| Work in process | 528 | 485 | 596 |
| Finished goods | 1,051 | 787 | 869 |
| | \$2,421 | \$1,786 | \$2,064 |

At December 31, 2011, May 31, 2011 and May 31, 2010, the Company maintained reserves for excess and obsolete inventories of \$606,000, \$409,000 and \$359,000, respectively.

NOTE G– BUSINESS COMBINATION

On August 19, 2011, the Company, through its newly formed subsidiary, Vasomedical Global, signed an agreement to purchase Life Enhancement Technology Limited and Biox Instruments Co., Ltd., both of which are based in the People's Republic of China.

On September 2, 2011, Vasomedical Global successfully completed the purchase of all the outstanding capital stock of privately-held Fast Growth Enterprises Limited ("FGE"), a British Virgin Islands company that owns subsidiaries

which own and control Life Enhancement Technology Limited (“LET”) and Biox Instruments Co. Ltd. (“Biox”), respectively, as per the stock purchase agreement signed on August 19, 2011. The consideration of this acquisition includes a cash payment of \$1 million as well as the issuance of 5 million restricted shares of the Company’s common stock, up to 2.4 million shares of common stock contingently issuable upon the achievement of certain operating performance targets, and warrants covering 1.5 million shares of common stock.

Vasomedical, Inc. and Subsidiaries

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LET, based in Foshan, Guangdong, China, has been Vasomedical's supplier for its proprietary Enhanced External Counterpulsation (EECP®) systems, including certain Lumenair systems and all AngioNew® systems. Biox, a developer and manufacturer of ambulatory monitoring devices in China, is located in Wuxi, Jiangsu, China, and has been Vasomedical's partner on the BIOX series ECG Holter recorder and analysis software as well as ambulatory blood pressure monitoring systems. Vasomedical has obtained FDA clearance to market these products in the United States. The acquisition of LET provides Vasomedical with consolidated technical and manufacturing capability in its EECP business which should significantly increase gross margins and enable the Company to meet anticipated increasing demand for its EECP systems. Management believes the acquisition of Biox greatly enhances Vasomedical's distribution network, technology and product portfolio, and with combined market and sales efforts of the two companies, should help improve performance and profitability of Vasomedical's equipment segment.

The operating results of FGE from September 2, 2011 to December 31, 2011 are included in the accompanying Consolidated Statement of Operations and Comprehensive Income (Loss) and Cash Flows for the seven months ended December 31, 2011. The accompanying Consolidated Balance Sheet as of December 31, 2011 reflects the acquisition of FGE, effective September 2, 2011. The acquisition date fair value of the total consideration transferred was \$3.979 million, which consisted of the following:

(in thousands)

| | |
|---|---------|
| Cash | \$1,000 |
| Vasomedical, Inc. common stock | 2,100 |
| Vasomedical, Inc. warrants to purchase common stock | 304 |
| Contingent issuance of Vasomedical, Inc. common stock | 575 |
| Total purchase price | \$3,979 |

The fair value of the common shares issued and the contingently issuable common shares was based on the closing price of the shares on September 2, 2011, as quoted on the Nasdaq OTC pink sheets, which was \$0.42 ("closing price"). The fair value of the warrants issued was computed using a Black Scholes Merton option pricing model, which utilized the following assumptions: expected term of two years which is the contractual term of the warrants; risk-free rate of 0.20%; 0% expected dividend yield; 100.67% expected volatility; the closing price; and an exercise price of \$0.50. The fair value of the contingent consideration recognized on the acquisition date was estimated based on a probability model.

In accordance with Accounting Standards Codification ("ASC") 805, Business Combinations ("ASC 805"), the total purchase consideration is allocated to the net tangible and identifiable intangible assets acquired and liabilities assumed based on their estimated fair values as of September 2, 2011 (the acquisition date). The purchase price was allocated based on the information currently available, and may be adjusted after obtaining more information regarding, among other things, asset valuations, liabilities assumed, and revisions of preliminary estimates. The following table summarizes the estimated fair values of the assets acquired and liabilities assumed at the acquisition date:

(in thousands)

| | |
|--|-------|
| Cash and cash equivalents | \$442 |
| Accounts receivable and other current assets | 283 |
| Inventories | 476 |
| Property and equipment | 32 |
| Goodwill | 3,939 |

| | |
|--|----------|
| Accounts payable and other current liabilities | (1,193) |
| Net assets acquired | \$3,979 |

The goodwill is attributable to the synergies expected to arise after the Company's acquisition of FGE as well as to FGE's projected growth and profitability. The goodwill is not expected to be deductible for tax purposes.

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Vasomedical, Inc. and Subsidiaries

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During the seven month period ended December 31, 2011, the Company expensed \$122,000 of acquisition-related costs. These costs are included in the line item Selling, General & Administrative costs in the accompanying Consolidated Statement of Operations and Comprehensive Income (Loss) and are comprised of accounting and legal fees.

After elimination of intercompany transactions, the amounts of revenue and net income of FGE included in the Company's Consolidated Statement of Operations and Comprehensive Income (Loss) for the seven ended December 31, 2011 was \$413,000 and \$35,000, respectively. Earnings per share was less than \$0.01. Prior to elimination of the intercompany transactions, the amounts of revenue and net income recognized by FGE from the acquisition date to December 31, 2011 was \$852,000 and \$350,000, respectively.

The following unaudited supplemental pro forma information presents the financial results as if the acquisition of FGE had occurred June 1, 2009 (amounts in thousands, except per share amounts):

(in thousands)

| | Seven Months Ended December 31, 2011 | Year ended May 31, 2011 | 2010 |
|-----------------------------------|---|----------------------------|----------|
| Revenue | \$ 23,600 | \$ 17,347 | \$ 5,129 |
| Net income (loss) | 5,046 | (3,405) | (1,499) |
| Basic earnings (loss) per share | 0.03 | (0.03) | (0.01) |
| Diluted earnings (loss) per share | 0.02 | (0.03) | (0.01) |

An adjustment was made to the unaudited pro forma financial information to reflect the acquisition-related costs in the year ended May 31, 2010.

NOTE H – PROPERTY AND EQUIPMENT

Property and equipment is summarized as follows:

(in thousands)

| | December 31, 2011 | May 31, 2011 | May 31, 2010 |
|---|----------------------|-----------------|-----------------|
| Office, laboratory and other equipment | \$ 1,205 | \$ 1,005 | \$ 943 |
| EECP® systems under operating leases or under loan for clinical trials | 795 | 800 | 823 |
| Furniture and fixtures | 203 | 194 | 149 |
| | 2,203 | 1,999 | 1,915 |
| Less: accumulated depreciation | (1,774) | (1,633) | (1,612) |

| | | | |
|-----------------------------|-------|-------|-------|
| Property and equipment, net | \$429 | \$366 | \$303 |
|-----------------------------|-------|-------|-------|

Depreciation expense amounted to approximately \$81,000, \$102,000, and \$77,000 for the seven months ended December 31, 2011 and for the years ended May 31, 2011 and 2010, respectively.

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Vasomedical, Inc. and Subsidiaries

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December 31, 2011, May 31, 2011 and 2010

NOTE I – GOODWILL AND OTHER INTANGIBLES

The change in the carrying amount of goodwill was as follows:

| | (in thousands) | Carrying Amount |
|------------------------------|----------------|--------------------|
| Balance at June 1, 2011 | | \$- |
| Acquisition of FGE (Note G) | | 3,939 |
| Balance at December 31, 2011 | | \$3,939 |

The Company owns eleven US patents including eight utility and three design patents that expire at various times between now and 2023. Costs incurred for submitting the applications to the United States Patent and Trademark Office and other foreign authorities for these patents have been capitalized. Patent costs are being amortized using the straight-line method over the related 10-year lives. The Company begins amortizing patent costs once a filing receipt is received stating the patent serial number and filing date from the Patent Office or other foreign authority.

The Company's other intangible assets consist of capitalized patent costs, as set forth in the following:

| | December 31, 2011 | May 31, 2011 | May 31, 2010 |
|--------------------------|----------------------|-----------------|-----------------|
| Patent Costs | | | |
| Costs | 469 | 469 | 469 |
| Accumulated amortization | (413) | (393) | (351) |
| | \$56 | \$76 | \$118 |

The other intangible assets are included in other assets on the Company's consolidated balance sheets.

Amortization expense amounted to \$20,000, \$43,000, and \$47,000 for the seven months ended December 31, 2011 and for the years ended May 31, 2011 and 2010, respectively.

NOTE J – DEFERRED REVENUE

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

| | For the seven months ended December 31, 2011 | For the years ended May 31, 2011 | 2010 |
|---|---|--|---------|
| Deferred revenue at the beginning of the period | \$11,922 | \$1,027 | \$1,288 |
| Additions: | | | |
| Deferred extended service contracts | 691 | 1,281 | 1,047 |
| Deferred in-service and training | 18 | 33 | 22 |

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| | | | |
|---|-----------|----------|----------|
| Deferred service arrangements | 29 | 98 | 71 |
| Deferred commission revenues | 23,121 | 19,558 | - |
| Recognized as revenue: | | | |
| Deferred extended service contracts | (639) | (1,239) | (1,254) |
| Deferred in-service and training | (25) | (23) | (30) |
| Deferred service arrangements | (48) | (61) | (117) |
| Deferred commission revenues | (19,842) | (8,752) | - |
| Deferred revenue at end of period | 15,227 | 11,922 | 1,027 |
| Less: current portion | 9,484 | 10,918 | 854 |
| Long-term deferred revenue at end of period | \$5,743 | \$1,004 | \$173 |

NOTE K – SALE-LEASEBACK

In August 2007, the Company sold its warehouse and corporate facility for \$1,400,000. Under the agreement, the Company is leasing back the property from the purchaser over a period of five years. The Company is accounting for the leaseback as an operating lease. The gain of \$266,000 realized in this transaction was deferred and is being amortized to income ratably over the term of the lease. The unamortized deferred gain of \$31,000, \$62,000 and \$115,000 as of December 31, 2011, May 31, 2011 and 2010, respectively, is shown as deferred gain on sale-leaseback of building in the Company's Consolidated Balance Sheets. The short-term portion of \$31,000 as of December 31, 2011, and \$53,000 as of May 31, 2011 and 2010, is shown in current liabilities and the long-term portion is in other long-term liabilities in the accompanying Consolidated Balance Sheets. The amount amortized in the seven months ended December 31, 2011 was \$31,000, and the amount amortized in each of the fiscal years ended May 31, 2011 and 2010 was \$53,000.

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NOTE L – WARRANTY LIABILITY

The changes in the Company’s product warranty liability are as follows:
(in thousands)

| | For the seven months ended December 31, 2011 | Years ended May 31, 2011 | 2010 |
|---|---|-----------------------------|-------|
| Warranty liability at the beginning of the period | \$30 | \$27 | \$23 |
| Expense for new warranties issued | 22 | 75 | 48 |
| Warranty claims | (32) | (72) | (44) |
| Warranty liability at the end of the period | 20 | 30 | 27 |
| Long-term warranty liability at the end of the period | \$- | \$- | \$- |

Warranty liability is included in accrued expenses and other liabilities on the Company’s consolidated balance sheets.

NOTE M – NOTES PAYABLE

At May 31, 2010, the Company had \$1,250,000 in notes payable to finance the start-up costs related to VasoHealthcare. Certain of the Company’s beneficial owners executed promissory notes with the Company on various dates during April and May of 2010 carrying an interest rate of 5% per annum and maturing on various dates in July 2010. These promissory notes were settled in June 2010 through the issuance of Series E preferred stock (see Note O).

NOTE N – RELATED-PARTY TRANSACTIONS

On June 21, 2007, we entered into a Securities Purchase Agreement with Kerns Manufacturing Corp. (“Kerns”). Concurrently with our entry into the Securities Purchase Agreement, we also entered into a Distribution Agreement and a Supplier Agreement with Living Data Technology Corporation (“Living Data”), an affiliate of Kerns. Pursuant to the Distribution Agreement, as amended, we became the exclusive worldwide distributor of the AngioNew EECP® systems manufactured through Living Data. The Distribution Agreement had an initial term extending through May 31, 2012. Effective September 2, 2011 the Company acquired Life Enhancement Technology (LET) (see Note G), the manufacturer of the AngioNew EECP® system. Consequently, the Distribution Agreement is no longer effective, and the Company wrote-off the remaining unamortized balance of Deferred Distributor Costs during the seven months ended December 31, 2011.

Pursuant to the Supplier Agreement, Living Data became our exclusive supplier of the external counterpulsation therapy systems that we market under the registered trademark EECP®. On February 28, 2010, the Supplier Agreement was terminated and, in connection with the termination, the Company purchased Living Data’s remaining inventory at cost (\$469,000), which was paid in 7,824,167 shares of common stock valued at the closing price on the termination date. Prior to termination, the Company purchased in fiscal 2010 additional EECP® therapy systems for \$40,000 from Living Data. Payment terms on certain purchases prior to 2010, plus \$3,000 in commissions for sales of

certain BIOX products, leave a balance of \$0, \$266,000, and \$240,000 in Trade Payable due to Related Party on the accompanying Consolidated Balance Sheets as of December 31, 2011, May 31, 2011 and May 31, 2010, respectively. The payable balance due Living Data included interest charges of \$24,000 at May 31, 2011 and was satisfied through a cash payment in August 2011.

On February 28, 2011, David Lieberman and Edgar Rios were appointed by the Board of Directors as directors of the Company. Mr. Lieberman, a practicing attorney in the State of New York, was appointed to serve as the Vice Chairman of the Board. He is currently a senior partner at the law firm of Beckman, Lieberman & Barandes, LLP, which firm performs certain legal services for the Company. Fees of approximately \$166,000 were billed by the firm for the seven months ended December 31, 2011, at which date no amounts were outstanding.

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Mr. Rios currently is President of Edgery Consultants, LLC, and was appointed a director in conjunction with the Company's consulting agreement with Edgery Consultants, LLC. The consulting agreement (the "Agreement") between the Company and Edgery Consultants, LLC ("Consultant") commenced on March 1, 2011 and runs for a two year term.. The Agreement provides for the engagement of Consultant to assist the Company in seeking broader reimbursement coverage of EECF® therapy. More specifically, Consultant will be assisting the Company in the following areas:

1. Engaging the adoption of EECF® therapy as a first line option for FDA cleared indications as it relates to CCS Class III/IV angina with a major commercial healthcare third-party payer.
2. Engaging a major commercial healthcare payer to formally collaborate and co-sponsor a study with Vasomedical for the efficacy, efficiency and/or cost effectiveness of the EECF® therapy for NYHA Class II/III heart failure.
3. Engaging final approval from the Centers for Medicare and Medicaid Services ("CMS") of EECF® therapy as a first line treatment for CCS Class III/IV angina.
4. Engaging final approval from CMS to extend coverage and provide for the reimbursement of EECF® therapy for CCS Class II angina; and
5. Engaging final approval from CMS to extend coverage and provide for the reimbursement of EECF® therapy for NYHA Class II/III heart failure.

In consideration for the services to be provided by Consultant under the Agreement, the Company has agreed to issue to Consultant or its designees, approximately 10% of the outstanding capital stock of the Company, of which the substantial portion (in excess of 82%) is performance based as referenced above. In conjunction with the Agreement, 3,000,000 shares of restricted common stock valued at \$1,020,000 were issued in March 2011. In connection with the Agreement, Mr. Lieberman received 600,000 of these restricted shares. The Company has recorded the fair value of the shares issued to Consultant as a prepaid expense and is amortizing the cost ratably over the two year agreement. The unamortized value is reported as Deferred Related Party Consulting Expense in our accompanying Consolidated Balance Sheets as of December 31, 2011 and May 31, 2011.

During the seven months ended December 31, 2011, a director performed consulting services for the Company aggregating approximately \$95,000, and the Company accrued dividends of \$15,000 on Series E Preferred Stock (see Note O) to directors, management, and other related parties of the Company.

During fiscal 2011, the Company sold, or issued as dividends, 246,870 shares of Series E Preferred Stock (see Note O) to directors, management, and other related parties of the Company. In addition, two directors performed consulting services for the company during fiscal 2011, aggregating approximately \$57,000.

Through the Company's acquisition of FGE in September 2011, it assumed the liability for \$288,000 in unsecured notes payable to the President of LET and his spouse, of which \$95,000 was repaid in December 2011, and \$190,000, bearing interest at 6% per annum, was paid in full in March 2012. In addition, \$10,000 in pre-acquisition earnings were distributed to current BIOX management and during the seven months ended December 31, 2011. The Company also recorded \$196,000 in loans and advances made to officers of FGE during the seven months ended December 31, 2011. These loans are short term and do not bear interest.

NOTE O – STOCKHOLDERS' EQUITY AND WARRANTS

Common stock and warrants

See Note N for discussion of common stock issued in fiscal 2011 and 2010 in connection with related party agreements. The Company also issued 1,151,492, 1,861,279, and 2,603,960 shares of common stock to directors, officers, employees, and/or consultants during the seven months ended December 31, 2011 and for the fiscal years 2011 and 2010, respectively.

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On July 19, 2005, we granted warrants for the purchase of 2,254,538 shares of common stock to investors and consultants. The warrants, with an exercise price of \$0.69 per share for a term of five years, expired unexercised on July 19, 2010.

On June 21, 2007, a five-year warrant to purchase 4,285,714 shares of our common stock at an initial exercise price of \$0.08 per share was issued to Kerns under the Securities Purchase Agreement. Additionally, we granted warrants for the purchase of 428,571 shares of common stock to a consultant in conjunction with the Kerns Securities Purchase Agreement. The initial exercise price was \$0.07 per share for a term of five years, and a cashless exercise was made in April 2011 resulting in the issuance of 383,790 shares of common stock.

In September 2011, the Company issued 5,000,000 shares of restricted common stock and a two year common stock purchase warrant for 1,500,000 shares at an exercise price of \$0.50 per share as partial consideration for the acquisition of FGE (see Note G). In addition, up to 2,400,000 shares of common stock are contingently issuable should FGE attain certain operating targets for the twelve months ending December 31, 2011. The Company is completing its evaluation of FGE's calendar year 2011 results and believes it is likely that the targets have been met.

The aggregate value of the aforementioned noncash consideration relative to the FGE acquisition was \$2,979,000 (see Note G for valuation assumptions and methodology).

Warrant activity for the seven months ended December 31, 2011 and for the years ended May 31, 2011 and 2010 is summarized as follows:

| | Employees | Consultants | Total | Weighted Average Price |
|---|-----------|-------------|-------------|------------------------------|
| Balance at May 31, 2009 | - | 6,968,823 | 6,968,823 | \$0.27 |
| Warrants expired | - | - | - | |
| Warrants issued | - | - | - | |
| Balance at May 31, 2010 | - | 6,968,823 | 6,968,823 | \$0.27 |
| Warrants expired | - | (2,254,538) | (2,254,538) | \$0.69 |
| Warrants issued | - | - | - | |
| Warrants exercised | - | (428,571) | (428,571) | \$0.07 |
| Number of shares exercisable at May 31, 2011 | - | 4,285,714 | 4,285,714 | \$0.08 |
| Warrants expired | - | - | - | |
| Warrants issued | - | 1,500,000 | 1,500,000 | \$0.50 |
| Warrants exercised | - | - | - | |
| Number of shares exercisable at December 31, 2011 | - | 5,785,714 | 5,785,714 | \$0.19 |

Preferred stock

At December 31, 2011, May 31, 2011 and 2010, the Company had 1,000,000 shares of preferred stock authorized. During the year ended May 31, 2011 the Company issued an aggregate 314,649 shares of its Series E preferred stock. 78,123 of the shares were issued to cover the cancellation of the notes payable outstanding at May 31, 2010

(see Note M). There were 299,024 shares of Series E preferred stock issued and outstanding at May 31, 2011 and no shares issued and outstanding at December 31, 2011 and May 31, 2010.

On June 24, 2010, the Company filed a Certificate of Designations of Preferences and Rights of Series E Convertible Preferred Stock ("Certificate of Designations"), as authorized by the Board of Directors, designating 350,000 shares of its 1,000,000 shares of preferred stock as Series E Convertible Preferred Stock ("Series E Preferred"). The conversion rights of the Series E Preferred are that each share will be convertible at any time on or after January 1, 2011, at the holder's option into 100 shares of common stock (an exercise price of \$.16 per share of common stock, the "Conversion Price"), subject to anti-dilution adjustment as set forth below. Each share of outstanding Series E Preferred Stock shall automatically be converted into shares of common stock on or after July 1, 2011, at the then effective applicable conversion ratio, if, at any time following the Issuance Date, the price of the common stock for any 30 consecutive trading days equals or exceeds three times the Conversion Price and the average daily trading volume for the Company's common stock for the 30 consecutive trading days exceeds 250,000 shares.

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Pursuant to its conversion terms, the Series E Preferred was deemed automatically converted to common stock effective July 1, 2011. As of December 31, 2011, 29,956,100 shares of common stock had been issued for 299,561 shares of Series E Preferred, with 712,350 shares of common stock yet to be issued.

For the seven months ended December 31, 2011 and the year ended May 31, 2011, the Company recorded dividends totaling \$1,221,000 and \$429,000, respectively. Included in these amounts is the recognition of the value of the embedded beneficial conversion feature of the Series E Preferred, which reflects the difference between the conversion price and the market price at time of investment. The amounts included in the dividends reported attributable to this beneficial conversion feature are \$1,201,000 and \$225,000 for the seven months ended December 31, 2011 and the year ended May 31, 2011, respectively. These are noncash dividends requiring no payment and ceased on conversion of the Series E Preferred to common stock.

Chinese subsidiaries dividends and statutory reserves

The payment of dividends by entities organized in China is subject to limitations. In particular, regulations in China currently permit payment of dividends only out of accumulated profits as determined in accordance with PRC accounting standards and regulations. Our Chinese subsidiaries are also required to set aside at least 10% of its after-tax profit based on PRC accounting standards each year to their general reserves until the accumulative amount of such reserves reaches 50% of their registered capital. These reserves are not distributable as cash dividends. In addition, they are required to allocate a portion of their after-tax profit to their staff welfare and bonus fund at the discretion of their respective boards of directors. Moreover, if any of our PRC subsidiaries incurs debt on its own behalf in the future, the instruments governing the debt may restrict its ability to pay dividends or make other distributions to us. Distribution of dividends from the Chinese operating companies to foreign shareholders is subject to a 10% withholding tax.

NOTE P - OPTION PLANS

1999 Stock Option Plan

In July 1999, the Company's Board of Directors approved the 1999 Stock Option Plan ("the 1999 Plan"), for which the Company reserved an aggregate of 2,000,000 shares of common stock. The 1999 Plan provides that a committee of the Board of Directors of the Company will administer it and that the committee will have full authority to determine the identity of the recipients of the options and the number of shares subject to each option. Options granted under the 1999 Plan may be either incentive stock options or non-qualified stock options. The option price shall be 100% of the fair market value of the common stock on the date of the grant (or in the case of incentive stock options granted to any individual principal stockholder who owns stock possessing more than 10% of the total combined voting power of all voting stock of the Company, 110% of such fair market value). The term of any option may be fixed by the committee but in no event shall exceed ten years from the date of grant. Options are exercisable upon payment in full of the exercise price, either in cash or in common stock valued at fair market value on the date of exercise of the option. In July 2000, the Company's Board of Directors increased the number of shares authorized for issuance under the 1999 Plan by 1,000,000 shares to 3,000,000 shares. In December 2001, the Board of Directors of the Company increased the number of shares authorized for issuance under the 1999 Plan by 2,000,000 shares to 5,000,000 shares.

In May 2006, the Board of Directors accelerated the vesting period for all unvested options to May 31, 2006.

The term for which options may be granted under the 1999 Plan expired July 12, 2009.

In fiscal 2010, options to purchase 30,000 shares of common stock under the 1999 Plan at an exercise price of \$1.69 were retired or cancelled.

In fiscal 2011, options to purchase 1,100,000 shares of common stock under the 1999 Plan at an exercise price ranging from \$0.09 to \$3.88 were retired or cancelled.

In the seven months ended December 31, 2011, options to purchase 54,000 shares of common stock under the 1999 Plan at an exercise price of \$3.96 were retired or cancelled.

2004 Stock Option and Stock Issuance Plan

In October 2004, the Company's stockholders approved the 2004 Stock Option and Stock Issuance Plan ("the 2004 Plan"), for which the Company reserved an aggregate of 2,500,000 shares of common stock. The 2004 Plan is divided into two separate equity programs: (i) the Option Grant Program under which eligible persons ("Optionees") may, at the discretion of the Board of Directors, be granted options to purchase shares of common stock; and (ii) the Stock Issuance Program under which eligible persons ("Participants") may, at the discretion of the Board of Directors, be issued shares of common stock directly, either through the immediate purchase of such shares or as a bonus for services rendered to the Company.

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Options granted under the 2004 Plan shall be non-qualified or incentive stock options and the exercise price is the fair market value of the common stock on the date of grant except that for incentive stock options it shall be 110% of the fair market value if the Optionee owns 10% or more of our common stock. The term of any option may be fixed by the Board of Directors or committee but in no event shall exceed ten years from the date of grant. Stock options granted under the 2004 Plan may become exercisable in one or more installments in the manner and at the time or times specified by the committee. Options are exercisable upon payment in full of the exercise price, either in cash or in common stock valued at fair market value on the date of exercise of the option. The term for which options may be granted under the 2004 Plan expires July 12, 2014.

Under the stock issuance program, the purchase price per share shall be fixed by the Board of Directors or committee but cannot be less than the fair market value of the common stock on the issuance date. Payment for the shares may be made in cash or check payable to us, or for past services rendered to us and all shares of common stock issued thereunder shall vest upon issuance unless otherwise directed by the committee. The number of shares issuable is also subject to adjustments upon the occurrence of certain events, including stock dividends, stock splits, mergers, consolidations, reorganizations, recapitalizations, or other capital adjustments. The term for which shares may be issued under the 2004 Plan expires July 12, 2014.

The 2004 Plan provides that a committee of the Board of Directors of the Company will administer it and that the committee will have full authority to determine and designate the individuals who are to be granted stock options or qualify to purchase shares of common stock under the 2004 Plan, the number of shares to be subject to options or to be purchased and the nature and terms of the options to be granted. The committee also has authority to interpret the 2004 Plan and to prescribe, amend and rescind the rules and regulations relating to the 2004 Plan.

In May 2006, the Board of Directors accelerated the vesting period for all unvested options to May 31, 2006.

In fiscal 2010, the Company's Board of Directors granted non-qualified stock options under the 2004 Plan to one director to purchase an aggregate of 200,000 shares of common stock, at an exercise price of \$0.08 per share (which represented the fair market value of the underlying common stock at the time of the respective grants) and the Company's Board of Directors granted non-qualified stock options under the 2004 Plan to one officer to purchase an aggregate of 250,000 shares of common stock, at an exercise price of \$0.08 per share (which represented the fair market value of the underlying common stock at the time of the respective grants). These options expire five years from the date of grant. In fiscal 2010, options to purchase 449,463 shares of common stock under the 2004 Plan at exercise prices ranging from \$0.57 to \$3.96 were retired or cancelled.

In fiscal 2011 there was no activity under the 2004 plan.

In the seven months ended December 31, 2011, there was no activity under the 2004 plan.

At December 31, 2011, there were 785,224 shares available for future grants under the 2004 Plan.

2010 Stock Option and Stock Issuance Plan

On June 17, 2010 the Board of Directors approved the 2010 Stock Plan (the "2010 Plan") for officers, directors, employees and consultants of the Company. The stock issuable under the 2010 Plan shall be shares of the Company's authorized but unissued or reacquired common stock. The maximum number of shares of common stock which may

be issued under the 2010 Plan is 5,000,000 shares.

The 2010 Plan is comprised of two separate equity programs, the Options Grant Program, under which eligible persons may be granted options to purchase shares of common stock, and the Stock Issuance Program, under which eligible persons may be issued shares of common stock directly, either through the immediate purchase of such shares or as a bonus for services rendered to the Company.

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The 2010 Plan provides that the Board of Directors, or a committee of the Board of Directors, will administer it with full authority to determine the identity of the recipients of the options or shares and the number of options or shares. Options granted under the 2010 Plan may be either incentive stock options or non-qualified stock options. The option price shall be 100% of the fair market value of the common stock on the date of the grant (or in the case of incentive stock options granted to any individual stockholder possessing more than 10% of the total combined voting power of all voting stock of the Company, 110% of such fair market value). The term of any option may be fixed by the Board of Directors, or its authorized committee, but in no event shall it exceed five years from the date of grant. Options are exercisable upon payment in full of the exercise price, either in cash or in common stock valued at fair market value on the date of exercise of the option.

As of December 31, 2011, 3,790,000 restricted shares of common stock were granted under the 2010 Plan to non-officer employees and consultants of the Company. As of December 31, 2011, 485,000 shares have been forfeited and 198,006 were withheld for withholding taxes. In September 2010, 650,000 restricted shares of common stock were granted under the 2010 Plan to officers of the Company. In September 2011, 475,000 restricted shares of common stock were granted under the 2010 Plan to an officer, of which 100,000 vested immediately with the remainder vesting over a three year period. No options were issued under the 2010 Plan during the seven months ended December 31, 2011 and fiscal 2011 or 2010.

Stock option and stock grant activity under all the plans for the seven months ended December 31, 2011 and for the years ended May 31, 2010 and 2011 is summarized as follows:

| | Outstanding Options | | | |
|--------------------------------------|----------------------------|------------------|-----------------------------------|---------------------------------|
| | Shares Available for Grant | Number of Shares | Range of Exercise Price per Share | Weighted Average Exercise Price |
| Balance at June 1, 2009 | 3,266,125 | 2,993,239 | 0.09 - \$3.96 | \$1.34 |
| Options granted | (450,000) | 450,000 | \$0.08 | \$0.08 |
| Options canceled | 479,463 | (479,463) | 0.57 - \$3.96 | \$1.24 |
| Expiration of 1999 Stock option plan | (2,510,364) | | | |
| Balance at May 31, 2010 | 785,224 | 2,963,776 | 0.08 - \$3.96 | \$0.57 |
| Options granted | - | - | | |
| Options canceled | - | (1,100,000) | 0.09 - \$3.88 | \$0.94 |
| Available under 2010 Plan | 920,000 | | | |
| Balance at May 31, 2011 | 1,705,224 | 1,863,776 | 0.08 - \$3.96 | \$0.34 |
| Options granted | - | - | | |
| Options canceled | - | (54,000) | \$3.96 | \$3.96 |
| Granted under 2010 Plan | (475,000) | - | | |
| Cancelled under 2010 Plan | 321,008 | - | | |
| Balance at December 31, 2011 | 1,551,232 | 1,809,776 | \$ | \$0.23 |

0.08 -
\$1.11

The following table summarizes information about stock options outstanding and exercisable at December 31, 2011:

| Range of Exercise Prices | Options Outstanding | | | Options Exercisable | |
|--------------------------------|---|--|--|---|--|
| | Number Outstanding at December 31, 2011 | Weighted Average Remaining Contractual Life (yrs.) | Weighted Average Exercise Price | Number Exercisable at December 31, 2011 | Weighted Average Exercise Price |
| 0.08 - \$0.58 | 1,689,776 | 4.3 | \$0.18 | 1,689,776 | \$0.18 |
| 0.71 - \$1.11 | 120,000 | 2.2 | \$1.04 | 120,000 | \$1.04 |
| | 1,809,776 | 4.2 | \$0.23 | 1,809,776 | \$0.23 |

There were 86,954,632 remaining authorized shares of common stock after reserves for all stock option plans and stock warrants.

Vasomedical, Inc. and Subsidiaries

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NOTE Q - INCOME TAXES

As of December 31, 2011, the recorded deferred tax assets were \$19,628,000, reflecting an increase of \$132,000 during the seven months ended December 31, 2011, which was offset by a valuation allowance of the same amount. The Company also recorded a deferred tax liability of \$112,000 as of December 31, 2011, which arose from pre-acquisition FGE operations, primarily related to revenue recognized for book prior to recognition for tax.

The Company's deferred tax assets are summarized as follows:

| | (in thousands) | | |
|-----------------------------------|----------------------|-----------------|-----------------|
| | December 31, 2011 | May 31, 2011 | May 31, 2010 |
| Net operating loss carryforwards | \$18,030 | \$19,301 | \$20,784 |
| Depreciation and amortization | 59 | - | (35) |
| Deferred rent | 3 | 5 | 6 |
| Deferred gain on sale of building | 12 | 21 | 39 |
| Allowance for doubtful accounts | 54 | 30 | 50 |
| Reserve for obsolete inventory | 165 | 139 | 122 |
| Tax credits | 358 | - | - |
| Expense accruals | 545 | - | - |
| Deferred revenue | 402 | - | - |
| Total gross deferred taxes | 19,628 | 19,496 | 20,966 |
| Valuation allowance | (19,628) | (19,496) | (20,966) |
| Net deferred tax assets | \$- | \$- | \$- |

At December 31, 2011, the Company had net operating loss carryforwards for federal and state income tax purposes of approximately \$45.1 million expiring at various dates from 2012 through 2031. In the seven months ended December 31, 2011 and for the fiscal years 2011 and 2010, approximately \$0.5 million, \$5.4 million and \$2.5 million, respectively, of net operating loss carryforwards expired. Future expirations of net operating loss carryforwards are approximately as follows:

(in thousands)

| Calendar Year | Amount |
|---------------|-----------|
| 2012 | \$ 6,100 |
| 2013 | 4,400 |
| 2014 | - |
| 2015 | - |
| 2016 | - |
| Thereafter | 34,600 |
| Total | \$ 45,100 |

Income tax expense for the seven months ended December 31, 2011 was \$276,000 and consisted mainly of Federal Alternative Minimum Tax and income tax in states with income in excess of applicable net operating loss carryforwards. Income tax expense for the year ended May 31, 2011 consists primarily of accruals for state taxes and adjustments for amounts paid or accrued in excess of actual income tax liabilities. The components of income tax

benefit for the year ended May 31, 2010 include federal research and development credits of approximately \$17,400. The remaining income tax benefit for the year ended May 31, 2010 consist primarily of federal and state refunds and adjustments for amounts paid or accrued in excess of actual income tax liabilities.

The Company has recorded a provision of \$500,000 for the potential liability that may arise from the business of FGE prior to its acquisition by the Company, which is included in accrued expenses and other liabilities on the Company's consolidated balance sheet as of December 31, 2011. Under the acquisition agreement of FGE by Vasomedical, the former shareholders of FGE have fully indemnified Vasomedical against any undisclosed liabilities and the Company believes that any liability that may arise should be recoverable from these former shareholders.

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Under current tax law, the utilization of tax attributes will be restricted if an ownership change, as defined, were to occur. Section 382 of the Internal Revenue Code provides, in general, that if an “ownership change” occurs with respect to a corporation with net operating and other loss carryforwards, such carryforwards will be available to offset taxable income in each taxable year after the ownership change only up to the “Section 382 Limitation” for each year (generally, the product of the fair market value of the corporation’s stock at the time of the ownership change, with certain adjustments, and a specified long-term tax-exempt bond rate at such time). The Company’s ability to use its loss carryforwards will be limited in the event of an ownership change.

The following is a reconciliation of the effective income tax rate to the federal statutory rate:

| | For the seven months ended December 31, 2011 % | For the years ended May 31, 2011 % | 2010 % |
|---|--|---|-----------|
| Federal statutory rate | 34.00 | (34.00) | (34.00) |
| State income taxes | 6.00 | (6.00) | (6.00) |
| Change in valuation allowance relating to operations | - | 40.00 | 40.00 |
| Utilizations of net operating loss carryforward | (40.00) | - | - |
| Foreign taxes | 1.17 | - | - |
| Alternative minimum tax | 2.10 | - | - |
| Other | 1.84 | 0.17 | (1.90) |
| | 5.12 | 0.17 | (1.90) |

NOTE R - COMMITMENTS AND CONTINGENCIES

Sales representation agreement

The GEHC Agreement is for an initial term of three years commencing July 1, 2010, subject to extension and also subject to earlier termination under certain circumstances. These circumstances include not materially achieving certain sales goals, not maintaining a minimum number of sales representatives, and various legal and GEHC policy requirements. Under the terms of the agreement, the Company is required to lease dedicated computer equipment from GEHC for connectivity to their network.

Facility Leases

On August 15, 2007, we sold our facility in Westbury, New York under a five-year leaseback agreement. VasoHealthcare also leases facilities in Greensboro, North Carolina pursuant to a lease which expires in May 2013. FGE leases facilities in Wuxi, China, pursuant to leases expiring in December 2013 and February 2015, and a facility in Foshan, China, pursuant to a lease that expires in April 2013.

Our Westbury lease expires in August 2012 at which time we will either extend the lease or seek nearby facilities. We believe that our current facility is adequate for foreseeable current and future needs and that there will be no difficulty in acquiring comparable facilities if we do not extend our current lease.

Vehicle Lease Agreement

In June 2011, the Company began taking deliveries under a closed-end master lease agreement for the provision of vehicles to the sales team of its Sales Representation segment. Vehicles obtained under the terms of the agreement are leased generally for a 36 month term, and payments are fixed for each year of the agreement, subject to readjustment at the beginning of the second and third year.

Future rental payments under these operating leases aggregate approximately as follows:

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For the years ended December 31,
(in thousands)

| | Vehicles | Facilities | Total |
|-------|----------|------------|-------|
| 2012 | \$265 | \$226 | \$491 |
| 2013 | 251 | 68 | 319 |
| 2014 | 129 | 3 | 132 |
| 2015 | - | 1 | 1 |
| Total | \$645 | \$298 | \$943 |

Employment Agreement

On March 21, 2011, the Company entered into an Employment Agreement with its President and Chief Executive Officer, for a three-year term ending on March 14, 2014 (the "Employment Agreement"). The Employment Agreement provides for annual compensation of \$200,000, eligibility for annual bonuses and long-term incentive awards, and certain severance benefits in the event of termination prior to the expiration date of the Employment Agreement.

Litigation

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

NOTE S - 401(K) PLAN

In April 1997, the Company adopted the Vasomedical, Inc. 401(k) Plan to provide retirement benefits for its employees. As allowed under Section 401(k) of the Internal Revenue Code, the plan provides tax-deferred salary deductions for eligible employees. Employees are eligible to participate in the next quarter enrollment period after employment. Participants may make voluntary contributions to the plan up to 15% of their compensation. In the seven months ended December 31, 2011 and for fiscal years 2011 and 2010, the Company made discretionary contributions of approximately \$25,000, \$27,000 and \$3,000, respectively, to match a percentage of employee contributions.

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NOTE T - TRANSITION PERIOD COMPARATIVE DATA (UNAUDITED)

The following table presents certain financial information for the seven months ended December 31, 2011 and 2010.

(in thousands except per share data)

| | For the seven months ended December 31, | |
|---|--|---------------------|
| | 2011 | 2010 (unaudited) |
| Statement of Operations Data: | | |
| Total revenues | \$23,489 | \$8,741 |
| Gross profit | 16,756 | 5,820 |
| Operating income (loss) | 5,189 | (2,445) |
| Total other income, net | 199 | 40 |
| Income (loss) before income taxes | 5,388 | (2,405) |
| Net income (loss) | 5,112 | (2,413) |
| Preferred stock dividends | (1,221) | (191) |
| Net income (loss) applicable to common stockholders | 3,891 | (2,604) |
| Comprehensive income (loss) | \$3,891 | \$(2,604) |
| Earnings (loss) per common share | | |
| - basic | \$0.03 | \$(0.02) |
| - diluted | \$0.03 | \$(0.02) |
| Weighted average common shares outstanding | | |
| - basic | 146,549 | 110,833 |
| - diluted | 153,657 | 110,833 |
| Statements of Cash Flows Data: | | |
| Cash used in operations | \$(5,179) | \$(1,032) |
| Net cash provided by (used in) investing activities | (638) | (132) |
| Net cash provided by (used in) financing activities | (95) | 3,783 |
| Effect of exchange rate differences on cash | 1 | - |
| Increase (decrease) in cash and cash equivalents | \$(5,911) | \$2,619 |

NOTE U – SUBSEQUENT EVENTS

Exercise of Warrant

In March 2012, Kerns Manufacturing Corp. exercised its warrant to purchase 4,285,714 shares of common stock at \$0.08 per share.

Employment Agreement of President and Chief Executive Officer

Pursuant to the terms of his employment agreement with the Company, at the recommendation of the Compensation Committee, the Executive Committee of the Company approved an increase in his annual salary to \$275,000, awarded him a \$50,000 bonus, and awarded him 500,000 restricted shares of common stock, of which one-half vests immediately and the remainder in one year.

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