VASOMEDICAL, INC
Form 10-K
March 27, 2014

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, DC 20549

FORM 10-K

[X] ANNUAL REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the fiscal year ended December 31, 2013
[ ] TRANSITION REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

Commission File No. 0-18105

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

Delaware (State or other jurisdiction of incorporation or organization)	11-2871434 (IRS Employer Identification No.)
180 Linden Avenue, Westbury, New York (Address of Principal Executive Offices)	11590 (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 (Title of Class)	OTCBB 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. o

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

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 x No o

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 x No o

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 o Accelerated filer o Non-accelerated filer o 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 o No x

The aggregate market value of common stock held by non-affiliates was approximately $40,945,000 based on the closing sales price of the common stock as quoted on the OTCBB on March 21, 2014.

At March 21, 2014, the number of shares outstanding of the issuer's common stock was 156,223,981.

DOCUMENTS INCORPORATED BY REFERENCE
Portions of the registrant’s definitive proxy statement in connection with its Annual Meeting of Stockholders to be held in May 2014, to be filed pursuant to Regulation 14A of the Securities Exchange Act of 1934, are incorporated by reference into Part III of this Annual Report on Form 10-K.

[THIS PAGE LEFT INTENTIONALLY BLANK]

VASOMEDICAL, INC.
INDEX TO FORM 10-K

Page

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 manageme 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

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 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 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.

In September 2011, the Company also 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 Chinese companies; and Vasomedical Solutions, Inc. was formed to manage and coordinate our EECP® equipment business as well as other medical equipment operations.

The Company will seek to achieve greater profitability by expanding our U.S. and international market product portfolio. In addition, the Company plans to actively pursue other accretive acquisitions or partnerships and to expand its sales representation business.

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 currently 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 had an initial term of three years and in 2012 was extended for an additional two years to June 30, 2015, 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 annual commission rate increases retroactively to January 1 when targets are met 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.

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 and ambulatory monitoring systems. 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.

Sales and Marketing

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

The sales and marketing efforts of our equipment segment are led by a vice president of sales and marketing as well as a vice president of national sales and service at Vasomedical Solutions, who supervises a team of sales managers covering various regions in the United States. We market our EECP® systems internationally through distributors in various countries throughout Europe, the Middle East, Africa, Asia and Latin America. We sell our Biox™-series ambulatory monitoring systems in China by a group of sales managers as well as through distributors covering various regions of China.

Competition

In the U.S. diagnostic imaging market, our main competitors are Siemens, Philips, Toshiba, and Hologic. 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.

Though we believe that we are the industry leader, in the United States our competitors in our EECP® business are Applied Cardiac Systems Inc., Cardiomedics Inc. and Scottcare Cardiovascular Solutions.

In the ambulatory monitoring system business, there are numerous competitors of various size and strength. The Biox™ series is among few from China with CE Mark certification, FDA clearances as well as Health Canada listing.

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 788,000 lives in the United States in 2010 and was responsible for 1 of every 3 deaths, according to Heart Disease and Stroke Statistics - 2014 Update: A Report from the American Heart Association (2014 Update). An estimated 83.6 million American adults, approximately 27% of the U.S. population, suffer from some form of cardiovascular disease.

We have FDA clearance to market our EECP® therapy for use in the treatment of (1) congestive heart failure and (2) chronic stable angina that is refractory to optimal anti-anginal medical therapy without options for revascularization (refractory angina). (See also Clearance by U.S. FDA, below.) 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 EECP® therapy is refractory angina symptoms.

Angina

Angina pectoris is the medical term for a recurring pain or discomfort in the chest, neck or arm due to coronary artery disease (CAD). The number of angina patients in the United States in 2010 is approximately 7.8 million, with 565,000 new cases in population of age 45 years or older, according to the 2014 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) 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 over 50 million beneficiaries in 2013, 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. 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. 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, and the symptoms include angina, shortness of breath, etc.

According to the 2014 Update, approximately 5.1 million adults in the United States were suffering from heart failure in 2010 and about 825,000 new cases of the disease occur each year in population of age 45 years or older. 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 and is expected to grow to approximately 8 million by 2030. 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. In the U.S. under the provisions of the current Patient Protection and Affordable Care Act (PPACA), starting in October 2011, every hospital’s 30-day hospital readmission rate for CHF, acute myocardial infarction (AMI) and pneumonia is evaluated by CMS and if a hospital is found to be in the lowest quartile in the annual ranking, CMS is authorized by the Hospital Readmission Reduction Program to penalize the hospital by reducing by 1% the hospital’s entire Medicare payment for the year. This 1% penalty will be applied for the calendar year 2013 and will be increased to 2% in 2014 and 3% in 2015.

We will continue to educate the marketplace that EECP® therapy is a therapy for the treatment of congestive heart failure and refractory angina and that patients with a 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. 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 congestive heart failure and refractory angina, 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. In addition, during the past several years, many studies have been conducted 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 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 and diabetes mellitus. 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 continue to sponsor clinical studies that may lead to regulatory clearance and reimbursement.

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 around 200 papers related to EECP® therapy published in peer-reviewed medical journals and in scientific and medical conferences all over the world since 1992. (In 2013 there were 21 new articles on EECP® therapy published in peer reviewed journals.) With only a few exceptions, these publications were 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.

Beneficial Clinical Outcomes

It has been well documented that the following benefits are sustained for up to three to five years:

- Increased myocardial perfusion to ischemic regions of the heart in patients with coronary artery disease (CAD);
- Improved cardiac functions and exercise capacity in patients with CAD and heart failure;
- Elimination or reduction in angina and heart failure symptoms;
- Improved CCS angina function class and heart failure NYHA function class;
- Reduced frequency of angina episodes and nitroglycerin usage in patients with refractory angina;
- Improved quality of life in patients with angina and heart failure.

Mechanisms of Action

During the past several years, the mechanisms of action of EECP® therapy have been the subject of many investigations, and independent research aiming to fully explain the precise scientific means by which EECP® therapy achieves its long-term beneficial effects and further studies continue 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. This 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, 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. In addition, it is now clear that during EECP® therapy the hemodynamic effect reduces circulating proinflammatory cytokines, arterial stiffness and smooth muscle cells proliferation and migration, slowing down the progression of atherosclerotic processes. These evidences supporting the mechanisms of action will lead to exploration of additional clinical applications of EECP® therapy.

Significant Economic Benefits

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 27 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 6-month ED visits per patient decreased by 78% after EECP® treatment, and 6-month hospitalizations were reduced by 73%. 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 of dollars in healthcare costs each year, and, as this is becoming an increasingly important issue of the nation's healthcare system, the Company is communicating to payers of these benefits as part of its campaign to expand reimbursement for EECP® therapy.

Registry data, while considered a valuable source of complementary clinical data, is retrospective and therefore deemed by researchers and others to be less convincing than prospective data or data from randomized and controlled clinical trials. 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 and ambulatory monitoring systems to treatment providers such as hospitals, clinics and physician private practices in the United States through our sales managers throughout the nation supervised by a vice president of U.S. sales and service at Vasomedical Solutions,. The efforts of our sales organization are supported by in-house marketing, administration and clinical educators who are responsible for training and certification of physicians and therapists, as well as updating customers on new clinical developments, especially relating to EECP® therapy. The Company also markets certain products, accessories and supplies through an online store.

Our domestic marketing activities support physician education and physician outreach programs, exhibition at national and regional medical conferences, as well as sponsoring 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.

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 initial service arrangement expires, we service our customers 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 authorized distributors with 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 renewal of the agreement, 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 (Ranexa®) and nesiritide (Natrecor®); as well as newer technologies such as gene therapy.

7

Government Regulations on EECP® Systems

We are subject to extensive regulation by numerous government regulatory agencies, including the U. S. 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

The Company's initial systems received FDA premarket notification (510(k)) clearance in 1995, with later models receiving clearance at various times between 2000 and 2004 as Class III preamendments devices.

On December 30, 2013, the FDA issued a final order that reclassified external counter-pulsating (ECP) devices for treatment of chronic stable angina for patients that are refractory to anti-anginal medical therapy and without options for revascularization from class III to class II (special controls).

In addition, FDA requires the filing of a premarket approval (PMA) or a notice of completion of a product development protocol (PDP) for ECP devices for other intended uses such as unstable angina, acute myocardial infarction, cardiogenic shock and congestive heart failure, which were previously cleared for marketing by means of 510(k) procedure. In accordance with federal regulations, ECP manufacturers may continue to commercially distribute their devices for these intended uses for a period of 90 days after the issuance of the final order. The devices may continue to be marketed only for refractory angina if a PMA or a notice of completion of a PDP is not filed before the end of the 90-day period.

In February, 2014 the Company filed documents with the FDA ensuring its 510(k) document file for EECP® Therapy systems is updated and consistent with the language currently required by the FDA for the indicated use as Class II devices. The Company continues to monitor the compliance requirements of the FDA on the proper and timely filing of documents to ensure the continuous marketing of EECP® Therapy systems for congestive heart failure, a Class III indication now requiring a PMA.

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 EECP® 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 Recommendation for EECP® Therapy

Medical professional societies periodically issue Practice Guidelines to their members and make them available publicly. The American College of Cardiology Foundation (ACCF) and the American Heart Association (AHA) have jointly produced guidelines in the area of cardiovascular since 1980. The ACCF/AHA practice guidelines are intended to assist healthcare providers in clinical decision making by describing a range of generally acceptable approaches to the diagnosis, management, and prevention of specific diseases or conditions.

On November 19, 2012 the ACCF/AHA Task Force on Practice Guidelines issued its new Guideline for the Diagnosis and Management of Patients With Stable Ischemic Heart Disease. EECP® therapy retained the same IIb Class of Recommendation (COR) rating it received in the ACC/AHA 2002 Guideline Update for the Management of Patients with Chronic Stable Angina. The new Guideline also gave EECP® therapy the same B rating for Level of Evidence (LOE) as the 2002 Guideline.

According to the Guideline, a class IIb rating maintains that procedures and treatments may be considered for patients. Additional studies with broad objectives are needed and further registry data would be helpful. This classification finds that the benefits of treatments are greater than or equal to the risk of treatment.

In August of 2013 The European Society of Cardiology issued new Guidelines on the Management of Stable Coronary Artery Disease (SCAD), in which EECP® Therapy was included for the first time and given a Class IIa Recommendation, meaning it "should be considered" as a treatment option as opposed to the "may be considered" recommendation of a IIb rating.

In the ACC/AHA 2005 Guidelines for the Diagnosis and Management of Chronic Heart Failure in the Adult, external counterpulsation was listed as one of the devices. The 2006 Comprehensive Heart Failure Practice Guideline by the Heart Failure Society of America does not include any comments on the use of external counterpulsation therapy for treating heart failure patients.

While EECP® therapy has not been approved by FDA for the treatment of stroke, AHA and The American Stroke Association (ASA) recommended "extracorporeal counterpulsation" with a IIb rating in its Guidelines for the Early Management of Patients With Acute Ischemic Stroke published in March 2013, which stated that "augmentation of cerebral collateral blood flow is a compelling concept that may hold promise in the treatment of acute ischemic stroke."

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, heart failure and some off-label applications continue to appear in presentations at major scientific meetings, in peer-reviewed publications, as well as on educational academic and patient oriented web sites each year. We continue to believe that new evidences from completed and ongoing studies regarding the efficacy of EECP® therapy and its long lasting effect will be sufficient to warrant modification to a more favorable recommendation level in practice guidelines. This would lead to 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 over 50 million beneficiaries now, issued a national coverage policy under HCPCS code G0166 for the use of the EECP® therapy system. The policy provided coverage for the use of the therapy

… 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 2014 national average payment rate per hourly EECP® therapy session in the physician office setting and the hospital outpatient facility is $137 and $106, respectively. Actual reimbursement rates vary throughout the country and range from $120 to $194 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 2005, as in the summary below:

Year	Physician Office	Hospital
2005	$138	$102
2006	$138	$104
2007	$147	$107
2008	$156	$109
2009	$150	$102
2010	$148	$104
2011	$153	$102
2012	$151	$94
2013	$144	$99
2014	$137	$106

If there were any material change in the availability of Medicare coverage, or if the reimbursement level for treatment procedures using the EECP® 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 EECP® 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 several years, we have started an initiative campaigning for a positive medical necessity decision in support of the use of EECP® therapy in the treatment of heart failure. At the same time, 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.

Coverage with Other Third-Party Payers

Since the establishment of reimbursement for EECP® therapy by the federal government, an increasing number of private third-party payers have routinely provided coverage for the use of EECP® 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 EECP® therapy for the treatment of CHF. On the other hand, there are private insurance carriers that continue to adjudicate EECP® 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 EECP® treatment that include CHF patients.

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 EECP® 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 EECP® 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. While there has been some progress with these projects to gain government and private insurance coverage in a few countries 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 from Biox Instruments Co. Ltd., based in Wuxi, China, for the BIOXTM 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, as well as the associated analysis and reporting software. The Company now offers a complete line of BIOXTM series diagnostic products for ambulatory monitoring needs.

In September 2011, the Company acquired the company that controls Biox and now includes its operations in the consolidated financial results. In March 2014, Biox annouced that the new MobiCare™ wireless multi-parameter patient monitoring system had received China FDA approval for marketing. The Company is in the process of preparing application for FDA clearance and CE Mark certification for the MobiCare™ system. In combination with Biox, the Company is also promoting its joint engineering design and manufacturing capabilities for potential OEM opportunities as well as pursuing international sales opportunities for the product line through its global distribution channel.

The global market for ambulatory monitoring systems is rapidly growing ; for example, the sales for ECG Holter systems worldwide is projected to reach $162.7 million by 2017, according to a research report by Global Industry Analysis, Inc. While there are multiple competitors in the marketplace, we believe that due to the many advantages of our products including certain innovative features, reasonable pricing, high production and regulation standards, and through our sales and marketing efforts in niche markets, we should increase sales revenue and create opportunities for all products the Company manufactures or distributes.

Strategic Objectives

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

a) Maintain and grow our equipment business, by

i) Continuing to align the cost structure with revenue growth; and

ii) Increasing our efforts to grow international sales of all our device offerings; and

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; and

iii) Pursuing accretive acquisitions of and partnerships with medical device manufacturers to expand our product portfolio.

c) Work with all stakeholders to expand reimbursement coverage for EECP® therapy and to explore new applications, 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 and to explore 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 through 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” , “VasoGlo “VasoSolutions” and “VasoHealthcare”.

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 and reporting.

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, 2013, we employed 215 full-time persons, of which 35 are employed through our facility in Westbury, New York, 92 through our VasoHealthcare subsidiary and 88 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 EECP® systems, and Vasomedical Global operates production facilities at the Life Enhancement Technology Co. Ltd. (LET) and Biox Instruments Co. Ltd. facilities in China. LET manufactures AngioNew® and Lumenair EECP® 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 EECP® 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.

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

Achieving profitable operations is dependent on several factors.

Our ability to achieve and sustain profitability 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 the significant amount of our revenue from our agreement with GEHC.

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 had an initial term of three years commencing July 1, 2010 and in 2012 was extended for two years to June 30, 2015, subject to extension and also subject to earlier termination under certain circumstances

A significant amount of our revenue and prior periods net income arise from activities under this contract. Moreover, our growth depends partially on the territories, customer segments and product modalities assigned to us 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.

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 continue to 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 Foundation and the American College of Cardiology Practice Guidelines continue to list EECP® as a therapy currently under investigation for treatment of heart failure and give EECP® a Level of Recommendation IIb rating 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 therapy’s benefits are greater than or equal to risk, but additional studies with broader objectives are needed and additional registry data would be helpful. 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 or effective 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(510(k)) or premarket approval (PMA) application 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, such as the final order on December 30, 2013 reclassifying ECP devices, 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 a PMA, 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 have foreign operations and are subject to the associated risks of doing business in foreign countries.

During the years ended December 31, 2013 and 2012, the Company had and continues to have operations in China. Operating internationally involves additional risks relating to such things as currency exchange rates, different legal and regulatory environments, political, economic risks relating to the stability or predictability of foreign governments, differences in the manner in which different cultures do business, difficulties in staffing and managing foreign operations, differences in financial reporting, operating difficulties, and other factors. The occurrence of any of these risks, if severe enough, could have a material adverse effect on the consolidated financial position, results of operations and cash flows of the Company.

Commercial law is still developing in China and there are limited legal precedents to follow in commercial transactions. There are many tax jurisdictions each of which may have changing tax laws. Applicable taxes include value added taxes (“VAT”), corporate income tax, and social (payroll) taxes. Regulations are often unclear. Tax declarations (reports) are subject to review and taxing authorities may impose fines, penalties and interest. These facts create risks in China.

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 or clearance by other jurisdictions. If we, or any of our 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 management, sales, 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.

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 cyclicality.

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 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, the Affordable Care Act was adopted which is designed to provide increased 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 the Affordable Care Act as well as 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.

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.

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 lease an 18,000 square foot headquarters and manufacturing facility at 180 Linden Avenue, Westbury, New York 11590 under a lease with a term that expires on August 31, 2015. The annual rental expense for the lease is approximately $139,000. 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 also lease approximately 1,500 square feet of office space in New York City under a lease that expires on May 31, 2017. The annual rent for this lease is approximately $40,000.

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, China and approximately 11,000 square feet at an annual cost of approximately $23,000 in Foshan, China.

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 $50,000. The current lease for the Greensboro, North Carolina office will expire by the end of May, 2014, and we do not believe there will be difficulty in relocating the office should we decide not to renew the lease.

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 OTCBB under the symbol VASO. The number of record holders of common stock as of March 21, 2014, 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.

	Year ended December 31, 2013		Year ended December 31, 2012	
	High	Low	High	Low
First quarter	$0.19	$0.17	$0.35	$0.19
Second quarter	$0.19	$0.17	$0.29	$0.18
Third quarter	$0.34	$0.17	$0.26	$0.19
Fourth quarter	$0.34	$0.25	$0.24	$0.15

The last bid price of the Company's common stock on March 21, 2014, was $.45 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 manageme 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 Annual 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 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. In September 2011, the Company also 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 Chinese companies; and Vasomedical Solutions, Inc. manages and coordinates our EECP® therapy business as well as other medical equipment operations.

Results of Operations – For the Years Ended December 31, 2013 and 2012

Net revenues increased by $3,650,000, or 12%, to $32,890,000 in the year ended December 31, 2013, from $29,240,000 in the year ended December 31, 2012. We reported a net loss of $1,145,000 for the year ended December 31, 2013 as compared to a net loss of $3,381,000 for the year ended December 31, 2012, a reduction of $2,236,000. Our net loss was $0.01 and $0.02 per basic and diluted common share for the years ended December 31, 2013 and 2012, respectively.

Revenues

Revenue in our Equipment segment increased 4% to $6,262,000, including $1,938,000 in revenue from FGE, for the year ended December 31, 2013 from $6,023,000, including $1,472,000 in FGE revenue, for the year ended December 31, 2012. Equipment segment revenue from equipment sales increased by $382,000, or 9%, to $4,573,000 for the year ended December 31, 2013 as compared to $4,191,000 for the year ended December 31, 2012. The increase in equipment sales is due primarily to a $466,000 increase in sales by FGE, as well as a 6% increase in domestic EECP® sales, mainly a net result of increased volume and lower average selling price, partially offset by a 9% decrease in international sales, driven by lower deliveries and lower average selling price.

We anticipate that demand for EECP® systems will remain soft unless there is greater clinical acceptance for the use of EECP® therapy or a favorable change in current reimbursement policies by CMS or third party payors. We also anticipate growth in the FGE revenue due to the growing medical device market in China, the introduction of new products, and our expanded international marketing effort.

Equipment segment revenue from equipment rental and services decreased 8% to $1,689,000 in the year ended December 31, 2013 from $1,832,000 in the year ended December 31, 2012. Revenue from equipment rental and services represented 27% of total Equipment segment revenue in the year ended December 31, 2013 and 30% in the year ended December 31, 2012. The decrease in revenue generated from equipment rentals and services is due primarily to decreased service revenues.

Commission revenues in the Sales Representation segment increased by $3,411,000, or 15%, to $26,628,000 in the year ended December 31, 2013, as compared to $23,217,000 in the year ended December 31, 2012. The increase was primarily the combined results of higher volume of GEHC equipment delivery in 2013 and higher commission rates. As discussed in Note B, the Company defers recognition of commission revenue until underlying equipment acceptance is complete. As of December 31, 2013, the Company recorded on its consolidated balance sheet a 22% increase in deferred commission revenue, to $16,666,000, of which $6,852,000 is long-term, compared to $13,686,000 in deferred commission revenue at December 31, 2012 of which $4,370,000 was long-term.

Gross Profit

The Company recorded gross profit of $22,513,000, or 68% of revenue, for the year ended December 31, 2013 compared to $20,594,000, or 70% of revenue, for the year ended December 31, 2012. The increase of $1,919,000 was due primarily to higher revenues in both the Sales Representation and Equipment segments, partially offset by a lower gross profit rate in the Sales Representation segment.

Equipment segment gross profit increased to $3,625,000, or 58% of Equipment segment revenues, for the year ended December 31, 2013 compared to $3,324,000, or 55% of Equipment segment revenues, for the year ended December 31, 2012 due to higher sales volume and improved margins resulting from FGE operations. Equipment segment gross profits are dependent on a number of factors including the mix of EECP® products and ambulatory monitoring devices, 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, as well as certain fixed period costs, including facilities, payroll and insurance.

Sales Representation segment gross profit was $18,888,000, or 71% of Sales Representation segment revenues, for the year ended December 31, 2013, an increase of $1,618,000, or 9%, from segment gross profit of $17,270,000, or 74% of segment revenue, for the year ended December 31, 2012. The increase in gross profit was due primarily to higher recognized revenue in 2013 as well as higher commission rates. Cost of commissions increased by $1,793,000, or 30%, to $7,740,000 for the year ended December 31, 2013, as compared to cost of commissions of $5,947,000 in 2012. Cost of commissions reflects commission expense associated with recognized commission revenues, and, starting in 2013, additional costs associated with the medical device excise tax imposed by the Patient Protection and Affordable Care Act, which was the primary cause of lower gross profit rates in 2013. Commission expense associated with deferred revenue is recorded as deferred commission expense until the related commission revenue is earned.

Operating Loss

Operating loss was $1,290,000 for the year ended December 31, 2013 compared to a loss of $3,508,000 for the year ended December 31, 2012, an improvement of $2,218,000. The decrease in operating loss was primarily attributable to the change from an operating loss in the Sales Representation segment of $153,000 in the year ended December 31, 2012 to operating income of $2,475,000 in that segment in the year ended December 31, 2013. The 2013 segment operating income reflected the impact of both higher commission rates and lower SG&A costs. Equipment segment operating loss in the year ended December 31, 2013 was $2,418,000, as compared to an operating loss of $1,806,000 in the year ended December 31, 2012. The increase in the Equipment segment operating loss was primarily due to higher SG&A costs, partially offset by higher gross profit. Operating loss after exclusion of non-cash expenses, decreased by $1,851,000 to $473,000 in the year ended December 31, 2013 from $2,324,000 in the same period of the prior year. Such non-cash expenses were comprised of depreciation, amortization, share-based compensation and other share-based arrangements, and decreased to $817,000 in the year ended December 31, 2013 from $1,184,000 in the year ended December 31, 2012.

Selling, general and administrative ("SG&A") expenses for the years ended December 31, 2013 and 2012 were $23,114,000, or 70% of revenues, and $23,526,000, or 80% of revenues, respectively, reflecting a decrease of $412,000 or approximately 2%. The decrease in SG&A expenditures in the year ended December 31, 2013 resulted primarily from lower costs incurred in conjunction with the extension of the GEHC agreement in 2013 than in 2012, which in turn led to decreased compensation expense in the Sales Representation segment, partially offset by an increase in the Equipment segment due mainly to higher sales and marketing expenses.

Research and development ("R&D") expenses of $689,000, or 2% of revenues (or 11% of Equipment segment revenues), for the year ended December 31, 2013 increased by $113,000, or 20%, from $576,000, or 2% of revenues (or 10% of Equipment segment revenues), for the year ended December 31, 2012. The increase is primarily attributable to an increase in development costs for our EECP® systems.

Interest and Other Income, Net

Interest and other income for the year ended December 31, 2013 and 2012, was $87,000 and $148,000, respectively, a decrease of $61,000. The decrease was due primarily to a $130,000 charge associated with a potential liability to a workers' compensation fund resulting from the 2007 closing of a trade association that previously provided workers' compensation for the Company and others, as well as lower interest income earned on the Company's cash balances, partially offset by higher government grants obtained by one of the Company's Chinese companies.

Amortization of Deferred Gain on Sale-leaseback of Building

The amortization of deferred gain on the sale-leaseback of building for the year ended December 31, 2013 and 2012 was $0 and $31,000, respectively. The gain resulted from the Company's sale-leaseback of its Westbury facility.

Income Tax Benefit (Expense), Net

During the year ended December 31, 2013, we recorded an income tax benefit of $58,000, as compared to an income tax expense of $52,000 in the year ended December 31, 2012. The Company utilized $0 and $0.8 million in net operating loss carryforwards for the years ended December 31, 2013 and 2012, respectively. Income tax expense decreased mainly due to a Federal tax refund received on a prior period return.

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.

Liquidity and Capital Resources

Cash and Cash Flow – For the year ended December 31, 2013

We have financed our operations from working capital. At December 31, 2013, we had cash and cash equivalents of $7,961,000, short-term investments of $111,000 and working capital of $6,716,000.

Cash used by operating activities was $1,504,000 during the year ended December 31, 2013, which consisted of the net loss after adjustments of $1,145,000 and cash used by changes in operating assets and liabilities of $359,000. The changes in the account balances primarily reflect increases in accounts and other receivables of $4,547,000, partially offset by a decrease in deferred revenue of $2,417,000. These changes in account balances are due mainly to the operations of our Sales Representation segment. At February 28, 2014 the Company's cash balances were approximately $13.8 million.

Cash used in investing activities during the year ended December 31, 2013 was $228,000, mainly related to the acquisition of equipment and software.

Cash used in financing activities during the year ended December 31, 2013 was $1,755,000 arising from the repurchase of common stock.

Liquidity

While the Company achieved substantial profitability in fiscal 2011, it has historically incurred operating losses and incurred losses for the years ended December 31, 2013 and 2012. The Company will seek to achieve profitability through our partner's higher delivery volume of equipment booked with our Sales Representation segment, through growth in our China operations, and by expanding our product portfolio. In addition, the Company plans to pursue other accretive acquisitions and partnerships in the international and domestic markets and to expand our sales representation business. We anticipate a return to profitability in 2014.

While we expect to generate positive operating cash flows in fiscal 2014, the progressive nature of the GEHC Agreement can cause related cash inflows to vary widely during the year.

Based on our operations through December 31, 2013 and our current business outlook for 2014, 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, 2015.

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, 2013, 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 more than 40 years specializing in corporation and securities law, was also 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. Mr. Rios currently is President of Edgary Consultants, LLC, and was appointed in conjunction with the Company's consulting agreement with Edgary Consultants, LLC.

The consulting agreement (the "Agreement") between Vasomedical, Inc. and Edgary Consultants, LLC ("Consultant") commenced on March 1, 2011 and ended on February 28, 2013. The Agreement provided for the engagement of Consultant to assist the Company in seeking broader reimbursement coverage of EECP® therapy.

In consideration for the services provided by Consultant under the Agreement, the Company had agreed to issue to Consultant or its designees, up to 18,500,000 shares of restricted common stock of the Company, 3,000,000 shares of which were issued in March 2011 and the balance was to be earned based on performance . Mr. Lieberman received 600,000 of these restricted shares from the initial issuance. No performance-based shares were issued and no additional compensation is expected to be paid under the agreement. Consultant, at its own expense, continued until August 2013 to investigate avenues through CMS and commercial payers to extend coverage and increased reimbursement for our EECP® therapy.

The Company paid $190,000 during the year ended December 31, 2012 for unsecured notes payable due to the president of LET and his spouse, collected $171,000 in loans and advances due from officers of FGE during the same period, and collected an additional $4,000 in such loans during the year ended December 31, 2013. These loans and advances are short term and do not bear interest. In addition, $30,000 in pre-acquisition earnings was distributed to current Biox management during 2012. At December 31, 2013, $3,000 remained payable to the president of LET and $21,000 remained due from officers of FGE.

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 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 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 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, 2013 and December 31, 2012. 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, 2013 and December 31, 2012. 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 utilizes the Black-Scholes option-pricing model.

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 February 2013, new guidance was issued that amends the current comprehensive income guidance. The new guidance requires entities to disclose the effect of each item that was reclassified in its entirety out of accumulated other comprehensive income and into net income on each affected net income line item. For reclassification items that are not reclassified in their entirety into net income a cross reference to other required disclosures is required. The adoption of this new guidance is to be applied prospectively, and for annual reporting periods beginning after December 15, 2012 and interim periods within those years. The adoption of this new guidance did not have an impact on the Company's consolidated financial position, results of operations or cash flows.

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, 2013 and have concluded that the Company's disclosure controls and procedures were effective as of December 31, 2013.

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 effective as of December 31, 2013.

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 Annual Report.

PART III

The information required by Part III is intended to be included in our definitive Proxy Statement, which will be filed with the Securities and Exchange Commission in connection with our 2014 Annual Meeting of Stockholders and is incorporated herein by reference.

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 Edgary Consultants, LLC. (12)
	(o)	Employment Agreement entered into as of March 21, 2011 between Vasomedical, Inc. and Jun Ma, as amended. (15)
	(p)	Stock Purchase Agreement dated as of August 19, 2011 among Vasomedical, Inc., Fast Growth Enterprises Limited (FGE) and the FGE Shareholders (13)
	(q)	Amendment to 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 June 20, 2012 (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%

(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

31

(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 10-K for the fiscal year ended May 31, 2011.
(14) Incorporated by reference to Report on Form 8-K dated June 20, 2012.
(15) Incorporated by reference to Reoprt on Form 10-K dated December 31, 2012.

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 26th day of March, 2014.

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 March 26, 2014, by the following persons in the capacities indicated:

/s/ Jun Ma Jun Ma	President, Chief Executive Officer and Director (Principal Executive Officer)
/s/ Michael Beecher Michael Beecher	Chief Financial Officer (Principal Financial Officer)
/s/ Simon Srybnik Simon Srybnik	Chairman of the Board
/s/ David Lieberman David Lieberman	Vice Chairman of the Board
/s/ Randy Hill Randy Hill	Senior Vice President and Director
/s/ Edgar Rios Edgar Rios	Director
/s/ Behnam Movaseghi Behnam Movaseghi	Director
/s/ Peter C. Castle Peter C. Castle	Director

Vasomedical, Inc. and Subsidiaries

INDEX TO CONSOLIDATED FINANCIAL STATEMENTS
For the years ended December 31, 2013 and 2012

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, 2013 and 2012, and the related consolidated statements of operations and comprehensive income (loss), changes in stockholders’ equity, and cash flows for each of the years in the two-year period ended December 31, 2013. 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 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 audit 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 audit 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 provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of the Company as of December 31, 2013 and 2012, and the results of its operations and its cash flows for each of the years in the two-year period ended December 31, 2013 in conformity with accounting principles generally accepted in the United States of America.

/s/ Rothstein Kass

New York, New York
March 27, 2014

Vasomedical, Inc. and Subsidiaries

CONSOLIDATED BALANCE SHEETS

(in thousands, except share data)

	December 31, 2013	December 31, 2012
ASSETS		
CURRENT ASSETS		
Cash and cash equivalents	$7,961	$11,469
Short-term investments	111	110
Accounts and other receivables, net of an allowance for doubtful accounts and commission adjustments of $3,764 at December 31, 2013 and $3,179 at December 31, 2012	13,570	9,145
Receivables due from related parties	21	25
Inventories, net	1,618	2,166
Deferred commission expense	2,312	2,480
Deferred related party consulting expense	-	85
Other current assets	338	236
Total current assets	25,931	25,716
PROPERTY AND EQUIPMENT, net of accumulated depreciation of $1,281 at December 31, 2013 and $1,161 at December 31, 2012	365	473
GOODWILL	3,303	3,212
OTHER ASSETS, net	3,918	2,980
	$33,517	$32,381
LIABILITIES AND STOCKHOLDERS' EQUITY		
CURRENT LIABILITIES		
Accounts payable	$597	$342
Accrued commissions	2,161	2,337
Accrued expenses and other liabilities	5,571	4,627
Sales tax payable	230	177
Deferred revenue - current portion	10,541	10,580
Deferred tax liability, net	112	112
Notes payable due to related party	3	3
Total current liabilities	19,215	18,178
LONG-TERM LIABILITIES		
Deferred revenue	7,478	5,022
Other long-term liabilities	359	171
Total long-term liabilities	7,837	5,193
COMMITMENTS AND CONTINGENCIES (NOTE P)		
STOCKHOLDERS' EQUITY		
Preferred stock, $.01 par value; 1,000,000 shares authorized; nil shares issued and outstanding at December 31, 2013, and December 31, 2012	-	-
Common stock, $.001 par value; 250,000,000 shares authorized; 164,705,382 and 162,917,996 shares issued at December 31, 2013 and December 31, 2012, respectively; 155,223,981 and		

162,917,996 shares outstanding at December 31, 2013 and		
December 31, 2012, respectively	165	163
Additional paid-in capital	61,508	61,229
Accumulated deficit	(53,561)	(52,416)
Accumulated other comprehensive income	108	34
Treasury stock, at cost, 9,481,401 and nil shares at December 31, 2013 and		
December 31, 2012, respectively	(1,755)	-
Total stockholders' equity	6,465	9,010
	$33,517	$32,381

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

Vasomedical, Inc. and Subsidiaries

CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE INCOME (LOSS)

(in thousands, except per share data)

	Year ended December 31,	
	2013	2012
Revenues		
Equipment sales	$4,573	$4,191
Equipment rentals and services	1,689	1,832
Commissions	26,628	23,217
Total revenues	32,890	29,240
Cost of revenues		
Cost of sales, equipment	1,785	1,791
Cost of equipment rentals and services	852	908
Cost of commissions	7,740	5,947
Total cost of revenues	10,377	8,646
Gross profit	22,513	20,594
Operating expenses		
Selling, general and administrative	23,114	23,526
Research and development	689	576
Total operating expenses	23,803	24,102
Operating loss	(1,290)	(3,508)
Other income (expense)		
Interest and other income (expense), net	87	148
Amortization of deferred gain on sale-leaseback of building	-	31
Total other income (expense), net	87	179
Loss before income taxes	(1,203)	(3,329)
Income tax benefit (expense)	58	(52)
Net loss	(1,145)	(3,381)
Other comprehensive income		
Foreign currency translation gain	74	34
Comprehensive loss	$(1,071)	$(3,347)
Loss per common share - basic and diluted	$(0.01)	$(0.02)
Weighted average common shares outstanding - basic and diluted	159,377	158,366

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

Vasomedical, Inc. and Subsidiaries

CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY

(in thousands)

	Common Stock		Treasury Stock		Additional		Accumulated Other	Total
	Shares	Amount	Shares	Amount	Paid-in Capital	Accumulated Deficit	Comprehensive Income	Stockholders' Equity
Balance at December 31, 2011	153,186	$ 153	-	$ -	$ 60,188	$ (49,065)	$ -	$ 11,276
Shares issued for acquisition	2,400	2			(2)	-	-	-
Share-based compensation	2,271	2			796	-	-	798
Shares not issued for employee tax liability	-	-			(103)	-	-	(103)
Shares granted for consulting agreements	63	-			13	-	-	13
Exercise of warrant	4,286	4			339	-	-	343
Issue shares for conversion of preferred shares	712	2			(2)	-	-	(0)
Other	-	-			-	30	-	30
Foreign currency translation gain (loss)	-	-			-	-	34	34
Net income/(loss)	-	-			-	(3,381)	-	(3,381)
Balance at December 31, 2012	162,918	$ 163	-	$ -	$ 61,229	$ (52,416)	$ 34	$ 9,010
Repurchase of shares	-	-	(9,481)	(1,755)	-	-	-	(1,755)
Share-based compensation	1,787	2			367	-	-	369
Shares not issued for employee tax liability	-	-			(88)	-	-	(88)
Foreign currency translation gain (loss)	-	-			-	-	74	74
Net income/(loss)	-	-			-	(1,145)	-	(1,145)
	164,705	$ 165	(9,481)	$ (1,755)	$ 61,508	$ (53,561)	$ 108	$ 6,465

Balance at December 31, 2013

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

Vasomedical, Inc. and Subsidiaries

CONSOLIDATED STATEMENTS OF CASH FLOWS
(in thousands)

	Year ended December 31,	
	2013	2012
Cash flows from operating activities		
Net loss	$(1,145)	$(3,381)
Adjustments to reconcile net loss to net cash		
(used in) provided by operating activities		
Depreciation and amortization	361	391
Amortization of deferred gain on sale-leaseback of building	-	(31)
Provision for doubtful accounts and commission adjustments	42	2
Share-based compensation	369	793
Amortization of deferred consulting expense	87	545
Changes in operating assets and liabilities:		
Accounts and other receivables	(4,547)	10,854
Receivables due from related parties	5	173
Inventories, net	545	249
Deferred commission expense	168	(648)
Other current assets	(103)	(17)
Other assets	(945)	(52)
Accounts payable	255	69
Accrued commissions	(177)	(1,479)
Accrued expenses and other liabilities	924	1,811
Sales tax payable	52	(179)
Deferred revenue	2,417	374
Other long-term liabilities	188	(43)
Net cash (used in) provided by operating activities	(1,504)	9,431
Cash flows from investing activities		
Purchases of property, equipment and software	(228)	(402)
Purchases of short-term investments	(111)	(70)
Redemption of short-term investments	111	70
Net cash used in investing activities	(228)	(402)
Cash flows from financing activities		
Proceeds from exercise of warrant	-	343
Repurchase of common stock	(1,755)	-
Repayment of notes payable due to related party	-	(190)
Net cash (used in) provided by financing activities	(1,755)	153
Effect of exchange rate differences on cash and cash equivalents	(21)	(7)
NET (DECREASE) INCREASE IN CASH AND CASH EQUIVALENTS	(3,508)	9,175
Cash and cash equivalents - beginning of year	11,469	2,294
Cash and cash equivalents - end of year	$7,961	$11,469
SUPPLEMENTAL DISCLOSURE OF CASH INFORMATION		
Interest paid	$-	$5

Income taxes paid	$69	$412
SUPPLEMENTAL SCHEDULE OF NON-CASH INVESTING AND FINANCING ACTIVITIES		
Inventories transferred to property and equipment,		
attributable to operating leases, net	$25	$9
Fair value of assets acquired	$-	$291
Liabilities assumed through acquisition	$-	$(291)

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

Vasomedical, Inc. and Subsidiaries

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE A – DESCRIPTION OF BUSINESS AND LIQUIDITY

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 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 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. In September 2011, the Company also 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 Chinese companies; and Vasomedical Solutions, Inc. manages and coordinates our EECP® equipment business as well as other medical equipment operations.

While the Company achieved substantial profitability in fiscal 2011, it has historically incurred operating losses and incurred a loss for the years ended December 31, 2013 and 2012. The Company will seek to achieve profitability through our partner’s higher delivery volume of equipment booked with our Sales Representation segment, through growth in our China operations, and by expanding our product portfolio. In addition, the Company plans to pursue other accretive acquisitions and partnerships in the international and domestic markets and to expand our sales representation business.

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.

Use of Estimates

The preparation of consolidated 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.

Vasomedical, Inc. and Subsidiaries

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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 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 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.

Vasomedical, Inc. and Subsidiaries

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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 the Sales Representation segment

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 EECP® 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 the year ended December 31, 2013, the Company granted 385,000 restricted shares of common stock valued at $91,700 to non-officer employees, vesting at various periods through June 2015, and granted 100,000 restricted shares of common stock valued at $18,000 to an officer, which vested immediately.

During the year ended December 31, 2012, the Company granted 2,392,500 restricted shares of common stock valued at $565,000 to non-officer employees in its VasoHealthcare subsidiary, vesting at various times through July 2013. In addition, in 2012 we granted 1,000,000 restricted shares of common stock valued at $250,000 to officers, of which 250,000 shares valued at $60,000 vested immediately, with the remainder vesting at various times through July 2014.

The Company did not grant any non-qualified stock options during the years ended December 31, 2013 or 2012.

Share-based compensation expense recognized for the years ended December 31, 2013 and 2012 was $369,000 and $793,000, respectively. Expense for other share-based arrangements was $87,000 and $545,000 for the years ended December 31, 2013 and 2012, respectively. Unrecognized expense related to existing share-based compensation and arrangements is approximately $91,000 at December 31, 2013 and will be recognized through June 2015.

Vasomedical, Inc. and Subsidiaries

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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.

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

	(in thousands)	
	For the year ended December 31, 2013	For the year ended December 31, 2012
Beginning Balance	$3,179	$2,163
Provision for losses on accounts receivable	68	(2)
Direct write-offs, net of recoveries	-	(2)
Commission adjustments	517	1,020
Ending Balance	$3,764	$3,179

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 result, believe that our receivable credit risk exposure is limited. For the years ended December 31, 2013 and 2012, 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 bank balances, which aggregated approximately $701,000 and $499,000 at December 31, 2013 and 2012, respectively.

Vasomedical, Inc. and Subsidiaries

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Our revenues were derived from the following geographic areas:

	(in thousands) For the year ended December 31, 2013	For the year ended December 31, 2012
Domestic (United States)	$29,431	$26,103
Non-domestic (foreign)	3,459	3,137
	$32,890	$29,240

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 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.

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.

Goodwill and Intangible Assets

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. Intangible assets consist of patent costs, customer lists and software. Intangible assets are amortized on a straight-line basis over their estimated useful lives, which range from 5 to 10 years. The Company capitalizes internal use software costs incurred during the application development stage. Costs related to preliminary project activities and post implementation activities are expensed as incurred. The Company capitalized $155,000 and $164,000 in software development costs for the years ended December 31, 2013 and 2012, respectively.

Impairment of Long-lived Assets

The Company reviews the recoverability of all long-lived assets, including the related useful lives, whenever events or changes in circumstances indicate that the carrying amount of a long-lived asset might not be recoverable. If required, the Company compares the estimated fair value determined by either the undiscounted future net cash flows or appraised value to the related asset's carrying value to determine whether there has been an impairment. If an asset is considered impaired, the asset is written down to fair value, which is based either on discounted cash flows or appraised values in the period the impairment becomes known. No assets were determined to be impaired for the years ended December 31, 2013 and 2012.

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 I)

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 K)

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.

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, 2013 and December 31, 2012. 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, 2013 and December 31, 2012. Generally, the Company is no longer subject to income tax examinations by major domestic taxing authorities for years before 2010. 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.

Vasomedical, Inc. and Subsidiaries

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Foreign Currency Translation Gain 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 accompanying consolidated balance sheet. For the years ended December 31, 2013 and 2012, comprehensive income (loss) includes gains of $74,000 and $34,000, respectively, which were 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 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 Loss Per Common Share

Basic loss per common share is based on the weighted average number of common shares outstanding without consideration of potential common stock. Diluted 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 year. Due to losses during the years ended December 31, 2013 and 2012, diluted loss per common share is equal to basic loss per common share for those years.

Vasomedical, Inc. and Subsidiaries

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The following table represents common stock equivalents that were excluded from the computation of diluted earnings per share for years ended December 31, 2013 and 2012, because the effect of their inclusion would be anti-dilutive.

	(in thousands)	
	Year ended December 31, 2013	Year ended December 31, 2012
Stock options	1,780	1,810
Warrants	-	1,500
Common stock grants	660	3,448
	2,440	6,758

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:

Adoption of New Standards

Other Comprehensive Income: Presentation of Comprehensive Income

In February 2013, new guidance was issued that amends the current comprehensive income guidance. The new guidance requires entities to disclose the effect of each item that was reclassified in its entirety out of accumulated other comprehensive income and into net income on each affected net income line item. For reclassification items that are not reclassified in their entirety into net income a cross reference to other required disclosures is required. The adoption of this new guidance is to be applied prospectively, and for annual reporting periods beginning after December 15, 2012 and interim periods within those years. The adoption of this new guidance did not have an impact on the Company's consolidated financial position, results of operations or cash flows.

Vasomedical, Inc. and Subsidiaries

NOTES TO 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:

	(in thousands)			
	As of or for the year ended December 31, 2013			
	Equipment Segment	Sales Representation Segment	Corporate	Consolidated
Revenues from external customers	$6,262	$ 26,628	$-	$ 32,890
Operating (loss) income	$(2,418)	$ 2,475	$(1,347)	$ (1,290)
Total assets	$6,922	$ 29,239	$(2,644)	$ 33,517
Accounts and other receivables, net	$933	$ 12,637	$-	$ 13,570
Deferred commission expense	$-	$ 3,978	$-	$ 3,978

	As of or for the year ended December 31, 2012			
	Equipment Segment	Sales Representation Segment	Corporate	Consolidated
Revenues from external customers	$6,023	$ 23,217	$-	$ 29,240
Operating loss	$(1,805)	$ (153)	$(1,550)	$ (3,508)
Total assets	$10,069	$ 23,615	$(1,303)	$ 32,381
Accounts and other receivables, net	$900	$ 8,245	$-	$ 9,145
Deferred commission expense	$-	$ 4,580	$-	$ 4,580

For the years ended December 31. 2013 and 2012, GE Healthcare accounted for 81% and 79% of revenue, respectively. Also, GE Healthcare accounted for $12.5 million, or 92%, and $8.1 million, or 89%, of accounts and other receivables at December 31, 2013 and December 31, 2012, 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.

Vasomedical, Inc. and Subsidiaries

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The following table presents information about the Company's assets measured at fair value as of December 31, 2013:

	(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, 2013
Assets				
Cash equivalents invested in money market funds (included in cash and cash equivalents)	$6,883	$-	$ -	$6,883
Investment in certificates of deposit (included in short-term investments)	111			111
	$6,994	$-	$ -	$6,994

The following table presents information about the Company's assets measured at fair value as of December 31, 2012:

	(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, 2012
Assets				
Cash equivalents invested in money market funds (included in cash and cash equivalents)	$9,124	$-	$ -	$9,124
Investment in certificates of deposit (included in short-term investments)	110			110
	$9,234	$-	$ -	$9,234

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

NOTE E – ACCOUNTS AND OTHER RECEIVABLES

The following table presents information regarding the Company's accounts and other receivables as of December 31, 2013 and 2012:

	(in thousands)	
	December 31, 2013	December 31, 2012

Trade receivables	$17,173	$12,193
Due from employees	161	131
Allowance for doubtful accounts and commission adjustments	(3,764)	(3,179)
Accounts and other receivables, net	$13,570	$9,145

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.

Vasomedical, Inc. and Subsidiaries

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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, 2013	December 31, 2012
Raw materials	$546	$909
Work in process	341	483
Finished goods	731	774
	$1,618	$2,166

At December 31, 2013 and 2012, the Company maintained reserves for excess and obsolete inventories of $803,000 and $576,000, respectively.

NOTE G – PROPERTY AND EQUIPMENT

Property and equipment is summarized as follows:

	(in thousands) December 31, 2013	December 31, 2012
Office, laboratory and other equipment	$1,049	$969
EECP® systems under operating leases		
or under loan for clinical trials	369	437
Furniture and fixtures	228	228
	1,646	1,634
Less: accumulated depreciation	(1,281)	(1,161)
Property and equipment, net	$365	$473

Depreciation expense amounted to approximately $213,000 and $193,000 for the years ended December 31, 2013 and 2012, respectively.

NOTE H – GOODWILL AND OTHER INTANGIBLES

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

	(in thousands) Carrying Amount
Balance at December 31, 2012	$3,212
Foreign currency translation	91
Balance at December 31, 2013	$3,303

Vasomedical, Inc. and Subsidiaries

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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

	(in thousands) December 31, 2013	December 31, 2012
Patents		
Costs	$469	$469
Accumulated amortization	(454)	(438)
	15	31
Customer lists		
Costs	800	800
Accumulated amortization	(267)	(152)
	533	648
Software		
Costs	696	541
Accumulated amortization	(424)	(386)
	272	155
	$820	$834

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

The Company owns eleven US patents including eight utility and three design patents that expire at various times through 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. Customer lists and software are amortized on a straight-line basis over their expected useful lives of seven and five years, respectively.

Amortization expense amounted to $169,000 and $198,000 for the years ended December 31, 2013 and 2012, respectively. Amortization of intangibles for the next five years is:

Amortization of Intangibles	2014	2015	2016	2017	2018
(in thousands)					
Amortization expense	$172	$167	$163	$142	$86

Vasomedical, Inc. and Subsidiaries

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE I – DEFERRED REVENUE

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

	(in thousands) For the year ended December 31, 2013	For the year ended December 31, 2012
Deferred revenue at the beginning of the year	$ 15,602	$ 15,227
Additions:		
Deferred extended service contracts	1,048	1,241
Deferred in-service and training	33	38
Deferred service arrangements	96	85
Deferred commission revenues	14,495	10,515
Recognized as revenue:		
Deferred extended service contracts	(991)	(1,113)
Deferred in-service and training	(28)	(38)
Deferred service arrangements	(74)	(87)
Deferred commission revenues	(12,162)	(10,266)
Deferred revenue at end of year	18,019	15,602
Less: current portion	10,541	10,580
Long-term deferred revenue at end of year	$ 7,478	$ 5,022

NOTE J – SALE-LEASEBACK

In August 2007, the Company sold its warehouse and corporate facility for $1,400,000. Under the agreement, the Company leased back the property from the purchaser over a period of five years and accounted for the leaseback as an operating lease. The gain of $266,000 realized in this transaction was deferred and amortized to income ratably over the term of the lease, which expired in August 2012. The amount amortized in the years ended December 31, 2013 and 2012 was $0 and $31,000, respectively.

NOTE K – WARRANTY LIABILITY

The changes in the Company's product warranty liability are as follows:

	(in thousands) For the year ended December 31, 2013	2012
Warranty liability at the beginning of the year	$26	$20
Expense for new warranties issued	57	63
Warranty claims	(50)	(57)
Warranty liability at the end of the year	33	26
Long-term warranty liability at the end of the year	$-	$-

Warranty liability is included in accrued expenses and other liabilities on the Company's Consolidated Balance Sheets.

NOTE L – RELATED-PARTY TRANSACTIONS

On June 21, 2007, we entered into a Securities Purchase Agreement with Kerns Manufacturing Corp. ("Kerns"), a stockholder of the Company. Under this agreement, a five-year warrant to purchase 4,285,714 shares of our common stock at an initial exercise price of $0.08 per shares was issued to Kerns. In March 2012, Kerns exercised its warrant and 4,285,714 shares of common stock were issued.

Vasomedical, Inc. and Subsidiaries

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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 also 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 $247,000 and $254,000 were billed by the firm for the years ended December 31, 2013 and 2012, respectively, at which dates no amounts were outstanding.

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. The consulting agreement (the "Agreement") between the Company and Edgary Consultants, LLC ("Consultant") commenced on March 1, 2011 and was for a two year term and expired on February 28, 2013. The Agreement provided for the engagement of Consultant to assist the Company in seeking broader reimbursement coverage of EECP® therapy.

In consideration for the services to be provided by Consultant under the Agreement, the Company agreed to issue to Consultant or its designees, up to 18,500,000 shares of restricted common stock of the Company, 3,000,000 of which, valued at $1,020,000, were issued in March 2011 and the balance was to be earned on performance. Mr. Lieberman received 600,000 of these restricted shares from the initial issuance. The Company recorded the fair value of the shares issued to Consultant as a prepaid expense and amortized 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, 2012. No performance-based shares were issued and no further compensation is expected to be paid in conjunction with the agreement.

During the year ended December 31, 2012, a former director performed consulting services for the Company aggregating approximately $10,000. Additionally, three directors received additional compensation totaling $150,000 for services rendered in connection with the extension of the GEHC contract.

The Company paid $190,000 during the year ended December 31, 2012 for unsecured notes payable due to the president of LET and his spouse, collected $171,000 in loans and advances due from officers of FGE during the same period, and collected an additional $4,000 in such loans during the year ended December 31, 2013. These loans and advances are short term and do not bear interest. In addition, $30,000 in pre-acquisition earnings was distributed to current BIOX management during 2012. At December 31, 2013, $3,000 remained payable to the president of LET and $21,000 remained due from officers of FGE.

NOTE M – STOCKHOLDERS' EQUITY AND WARRANTS

Common stock and warrants

See Note L for discussion of common stock issued in the year ended December 31, 2012 in connection with related party agreements. In addition, the Company issued 1,787,386 shares of common stock valued at $417,000 and 2,333,586 shares of common stock valued at $546,000 to directors, officers, employees, and consultants during the years ended December 31, 2013 and 2012, respectively.

In April 2013, the Company's Board of Directors authorized a share repurchase program of up to $1.5 million, which was subsequently increased in July 2013 to $2.0 million, of the Company's common stock. During the year ended December 31, 2013, the Company repurchased 9,481,401 shares at a cost of $1,755,000, which cost has been recorded as treasury stock in the accompanying consolidated balance sheet as of December 31, 2013.

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. In addition, up to 2,400,000 shares of common stock were contingently issuable should FGE attain certain operating targets for the twelve months ended December 31, 2011. In September 2012, the Company determined FGE had met its targets and issued 2,400,000 shares to the prior owners of FGE. The aggregate value of the aforementioned noncash consideration relative to the FGE acquisition was $2,979,000.

Vasomedical, Inc. and Subsidiaries

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Warrant activity for the years ended December 31, 2013 and 2012 is summarized as follows:

	Employees	Consultants	Total	Weighted Average Price
Number of shares exercisable at December 31, 2011	-	5,785,714	5,785,714	$0.19
Warrants expired				
Warrants issued				
Warrants exercised		(4,285,714)	(4,285,714)	$0.08
Number of shares exercisable at December 31, 2012	-	1,500,000	1,500,000	$0.50
Warrants expired		(1,500,000)	(1,500,000)	$0.50
Warrants issued		-	-	
Warrants exercised		-	-	
Number of shares exercisable at December 31, 2013	-	-	-	

Preferred stock

At December 31, 2013 and 2012, the Company had 1,000,000 shares of preferred stock authorized. There were no shares issued and outstanding at December 31, 2013 and 2012. Pursuant to its conversion terms, all outstanding Series E Convertible Preferred Stock ("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 yet to be issued. The remaining 712,350 shares were issued in 2012.

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. Based on People's Republic of China (PRC) accounting standards, our Chinese subsidiaries are also required to set aside at least 10% of after-tax profit each year to their general reserves until the accumulative amount of such reserves reaches 50% of the 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 N - 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.

Vasomedical, Inc. and Subsidiaries

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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.

During the year ended December 31, 2013, options to purchase 30,000 shares of common stock under the 1999 Plan at an exercise price ranging from $0.71 to $0.91 were retired.

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.

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 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.

There was no activity under the 2004 plan during the years ended December 31, 2013 and 2012.

At December 31, 2013, there were 785,224 shares available for future grants under the 2004 Plan.

F-22

Vasomedical, Inc. and Subsidiaries

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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.

In the year ended December 31, 2012, 500,000 restricted shares of common stock were granted under the 2010 Plan to officers of the Company, of which 250,000 shares vested immediately with the remainder vesting over a one year period. As of December 31, 2012, 355,000 additional shares were forfeited and 245,552 additional shares were withheld for withholding taxes.

During the year ended December 31, 2013, 85,000 restricted shares of common stock were granted under the 2010 Plan to employees of the Company, all of which vested immediately. As of December 31, 2013, 105,000 additional shares were forfeited and 204,662 additional shares were withheld for withholding taxes.

No options were issued under the 2010 Plan during the years ended December 31, 2013 and 2012.

2013 Stock Option and Stock Issuance Plan

On October 30, 2013, the Board of Directors approved the 2013 Stock Plan (the "2013 Plan") for officers, directors, employees and consultants of the Company. The stock issuable under the 2013 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 2013 Plan is 7,500,000 shares.

The 2013 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.

No shares were granted or options issued under the 2013 Plan during the years ended December 31, 2013 and 2012.

F-23

Vasomedical, Inc. and Subsidiaries

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Stock option and stock grant activity under all the plans for the years ended December 31, 2013 and 2012 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 December 31, 2011	1,551,232	1,809,776	0.08 - $$1.11	$0.23
Options granted	-			
Options canceled	-			
Granted under 2010 Plan	(500,000)			
Cancelled under 2010 Plan	600,552			
Balance at December 31, 2012	1,651,784	1,809,776	0.08 - $$1.11	$0.23
Options granted	-	-		
Options canceled under 1999 Plan	-	(30,000)		
Granted under 2010 Plan	(85,000)	-		
Cancelled under 2010 Plan	309,662	-		
Authorized under 2013 Plan	7,500,000			
Balance at December 31, 2013	9,376,446	1,779,776	0.08 - $$1.11	$0.22

The following table summarizes information about stock options outstanding and exercisable at December 31, 2013:

	Options Outstanding			Options Exercisable	
Range of Exercise Prices	Number Outstanding at December 31, 2013	Weighted Average Remaining Contractual Life (yrs.)	Weighted Average Exercise Price	Number Exercisable at December 31, 2013	Weighted Average Exercise Price
0.08 - $$0.58	1,689,776	2.3	$0.18	1,689,776	$0.18
$1.11	90,000	0.5	$1.11	90,000	$1.11
	1,779,776	2.2	$0.22	1,779,776	$0.22

There were 74,138,396 remaining authorized shares of common stock after reserves for all stock option plans and stock warrants.

NOTE O - INCOME TAXES

As of December 31, 2013, the recorded deferred tax assets were $19,041,000, reflecting an increase of $894,000 during the year ended December 31, 2013, which was offset by a valuation allowance the same amount. The Company also recorded a net deferred tax liability of $112,000 as of December 31, 2013 and 2012, which arose from pre-acquisition FGE operations, primarily related to revenue recognized for book prior to recognition for tax.

Vasomedical, Inc. and Subsidiaries

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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

	(in thousands) December 31, 2013	December 31, 2012
Net operating loss carryforwards	$17,155	$15,584
Depreciation and amortization	136	143
Allowance for doubtful accounts	66	50
Reserve for obsolete inventory	289	195
Tax credits	370	358
Expense accruals	196	482
Deferred revenue	829	1,335
Total gross deferred taxes	19,041	18,147
Valuation allowance	(19,041)	(18,147)
Net deferred tax assets	$-	$-

At December 31, 2013, the Company had net operating loss carryforwards for federal and state income tax purposes of approximately $42.9 million expiring at various dates from 2019 through 2033. Approximately $4.4 million and $6.1 million of net operating loss carryforwards expired in the years ended December 31, 2013 and 2012, respectively. Future expirations of net operating loss carryforwards are approximately as follows:

Calendar Year	(in thousands) Amount
2014	-
2015	-
2016	-
2017	-
2018	-
Thereafter	42,900
Total	$42,900

The Company recorded an income tax benefit of $58,000 for the year ended December 31, 2013 arising from a Federal refund of $97,000 related to a prior period amended return, partially offset by $52,000 in foreign income tax expense. Income tax expense for the year ended December 31, 2012 was $52,000 and consisted mainly of state income taxes.

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.

Vasomedical, Inc. and Subsidiaries

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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

	For the year ended	
	December 31, 2013	December 31, 2012
	%	%
Federal statutory rate	34.00	34.00
State income taxes	6.00	6.00
Change in valuation allowance relating to operations	-	-
Utilizations of net operating loss carryforward	(40.00)	(40.00)
Foreign taxes	4.32	0.20
Alternative minimum tax	(8.37)	(0.37)
Other	(0.77)	1.73
	(4.82)	1.56

The foreign tax effective rate increased mainly due to the expiration of certain tax advantages applicable to our Biox subsidiary. The alternative minimum tax (AMT) rate decreased due to a Federal refund on an amended prior period return.

NOTE P - COMMITMENTS AND CONTINGENCIES

Sales representation agreement

In June 2012, the Company concluded an amendment of the GEHC Agreement with GE Healthcare, originally signed on May 19, 2010. The amendment, effective July 1, 2012, extends the initial term of three years commencing July 1, 2010 to five years through June 30, 2015, 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, which expired in August 2012. In September 2012, the term of the lease was extended for an additional three years. The Company also leases offices in New York City under a five year agreement expiring May 2017. VasoHealthcare also leases facilities in Greensboro, North Carolina pursuant to a lease which expires in May 2014. FGE leases facilities in Wuxi, China, pursuant to leases expiring in February 2014 and March 2018, and a facility in Foshan, China, pursuant to a lease that expires in April 2016.

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.

F-26

Vasomedical, Inc. and Subsidiaries

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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

For the years ended December 31,

	(in thousands)		
	Vehicles	Facilities	Total
2014	$231	$276	$507
2015	64	215	279
2016	16	97	113
2017	-	66	66
2018	-	12	12
Total	$311	$666	$977

Employment Agreement

On March 21, 2011, the Company entered into an Employment Agreement with its President and Chief Executive Officer, Dr. Jun Ma, for a three-year term ending on March 14, 2014. The Employment Agreement currently provides for annual compensation of $275,000. Dr. Ma shall be eligible to receive a bonus 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 Employment Agreement further provides for reimbursement of certain expenses, and certain severance benefits in the event of termination prior to the expiration date of the Employment Agreement. Dr. Ma’s agreement, as modified, is for a continuing three year term, unless earlier terminated by the Company, but in no event can extend beyond March 21, 2019.

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.

Foreign operations

During the years ended December 31, 2013 and 2012, the Company had and continues to have operations in China. Operating internationally involves additional risks relating to such things as currency exchange rates, different legal and regulatory environments, political, economic risks relating to the stability or predictability of foreign governments, differences in the manner in which different cultures do business, difficulties in staffing and managing foreign operations, differences in financial reporting, operating difficulties, and other factors. The occurrence of any of these risks, if severe enough, could have a material adverse effect on the consolidated financial position, results of operations and cash flows of the Company.

Commercial law is still developing in China and there are limited legal precedents to follow in commercial transactions. There are many tax jurisdictions each of which may have changing tax laws. Applicable taxes include value added taxes ("VAT"), corporate income tax, and social (payroll) taxes. Regulations are often unclear. Tax declarations (reports) are subject to review and taxing authorities may impose fines, penalties and interest. These facts create risks in China.

F-27

Vasomedical, Inc. and Subsidiaries

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE Q - 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. In the years ended December 31, 2013 and 2012 the Company made discretionary contributions of approximately $62,000 and $81,000, respectively, to match a percentage of employee contributions.