NeuroMetrix, Inc.
Form 10-Q
August 08, 2008

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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended June 30, 2008

OR

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

For the transition period from to
Commission File Number 000-50856

NEUROMETRIX, INC.

(Exact name of registrant as specified in its charter)

Delaware	**04-3308180**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
62 Fourth Avenue, Waltham, Massachusetts	**02451**
(Address of principal executive offices)	(Zip Code)

(781) 890-9989

(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding twelve (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 ninety (90) days.

Yes ý No o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See the definitions of "accelerated filer", "large accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act (check one):

Large accelerated filer o	Accelerated filer ý	Non-accelerated filer o (Do not check if a	Smaller reporting company o

smaller reporting
company)

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes o No ý

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date: 13,773,855 shares of common stock, par value $0.0001 per share, were outstanding as of August 1, 2008.

NEUROMETRIX, INC.
FORM 10-Q
INDEX

PART I FINANCIAL INFORMATION

PART II OTHER INFORMATION

PART I

FINANCIAL INFORMATION

Item 1. Financial Statements

NeuroMetrix, Inc.

Balance Sheets

(Unaudited)

	June 30, 2008 (Consolidated)	December 31, 2007
Assets		
Current assets:		
Cash and cash equivalents	$ 13,513,856	$ 7,097,239
Short-term held-to-maturity investments	9,257,911	22,621,741
Restricted cash	45,000	45,000
Accounts receivable, net of allowance for doubtful accounts of $856,000 and $906,000 at June 30, 2008 and December 31, 2007, respectively	5,029,026	5,731,697
Inventories	6,145,290	5,354,338
Prepaid expenses and other current assets	1,072,268	710,159
Current portion of deferred costs	421,320	464,061
Total current assets	35,484,671	42,024,235
Restricted cash	408,000	1,458,598
Fixed assets, net	2,739,001	2,973,718
Long-term available-for-sale investment	442,835	1,058,255
Goodwill		5,833,464
Intangible assets, net	4,462,500	2,800,000
Deferred costs	158,973	226,304
Other long-term asset	55,082	
Total assets	$ 43,751,062	$ 56,374,574
Liabilities, Minority Interest and Stockholders' Equity		
Current liabilities:		
Accounts payable	$ 1,548,635	$ 2,627,889
Accrued compensation	1,726,283	2,127,546
Other accrued expenses	2,219,403	2,308,563
Current portion of deferred revenue	1,689,014	1,643,026
Current portion of capital lease obligation	12,900	12,900
Total current liabilities	7,196,235	8,719,924
Deferred revenue	618,470	891,958
Capital lease obligation net of current portion	11,825	18,275
Other long-term liabilities		14,546
Total liabilities	7,826,530	9,644,703
Minority interest	2,021,250	
Commitments and contingencies		
Stockholders' equity:		
Preferred stock, $0.001 par value, 5,000,000 shares authorized, none outstanding		
Common stock, $0.0001 par value; 50,000,000 shares authorized; 13,773,855 and 13,690,134 shares issued and outstanding at June 30, 2008 and December 31, 2007, respectively	1,377	1,369
Additional paid-in capital	111,702,948	110,235,835

Accumulated deficit	(77,801,043)	(62,065,588)
Accumulated other comprehensive loss		(1,441,745)
Total stockholders' equity	33,903,282	46,729,871
Total liabilities, minority interest and stockholders' equity	$ 43,751,062	$ 56,374,574

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

NeuroMetrix, Inc.

Statements of Operations

(Unaudited)

	Three Months Ended		Six Months Ended	
	June 30, 2008	June 30, 2007	June 30, 2008	June 30, 2007
	(Consolidated)		(Consolidated)	
Revenues:				
Medical equipment	$ 512,309	$ 1,223,173	$ 1,262,213	$ 2,502,377
Consumables	7,615,491	10,048,336	15,601,278	20,321,114
Other	365,371	204,000	727,635	409,804
Total revenues	8,493,171	11,475,509	17,591,126	23,233,295
Costs and expenses:				
Cost of revenues, excluding amortization	2,490,983	3,067,635	4,987,399	6,162,253
Research and development expenses	1,555,082	1,266,691	3,176,812	2,481,763
Sales and marketing expenses	4,016,725	6,019,947	9,626,973	11,995,885
General and administrative expenses	3,967,233	2,868,650	7,779,603	6,210,868
Charge for impaired goodwill			5,833,464	
Amortization of intangible assets	245,000		437,500	
Total costs and expenses	12,275,023	13,222,923	31,841,751	26,850,769
Loss from operations	(3,781,852)	(1,747,414)	(14,250,625)	(3,617,474)
Loss on available-for-sale investment	(1,401,146)		(2,057,165)	
Interest income	202,560	456,423	493,585	949,201
Loss before minority interest	(4,980,438)	(1,290,991)	(15,814,205)	(2,668,273)
Minority interest	52,500		78,750	
Net loss	$ (4,927,938)	$ (1,290,991)	$ (15,735,455)	$ (2,668,273)
Net loss per common share (basic and diluted):	$ (0.36)	$ (0.10)	$ (1.15)	$ (0.21)
Weighted average shares used to compute net loss per common share (basic and diluted):	13,693,449	12,611,880	13,691,792	12,608,673

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

NeuroMetrix, Inc.

Statements of Cash Flows

(Unaudited)

	Six Months Ended	
	June 30, 2008	**June 30, 2007**
	(Consolidated)	
Cash flows from operating activities:		
Net loss	$(15,735,455)	$ (2,668,273)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	911,544	222,501
Compensation expense associated with stock options	1,366,985	1,428,987
Provision for doubtful accounts	50,565	468,842
Amortization of (discount) premium on investments	(38,572)	10,683
Loss on available-for-sale investment	2,057,165	
Charge for impaired goodwill	5,833,464	
Minority interest	(78,750)	
Changes in operating assets and liabilities:		
Accounts receivable	652,106	982,573
Inventories	(790,952)	(1,551,219)
Prepaid expenses and other current assets	(362,109)	(107,522)
Other long-term asset	(55,082)	
Accounts payable	(1,079,254)	141,266
Accrued expenses and compensation	(490,423)	(2,084,646)
Other long-term liabilities	(14,546)	(29,091)
Deferred revenue and deferred costs	(117,428)	(33,384)
Net cash used in operating activities	(7,890,742)	(3,219,283)
Cash flows from investing activities:		
Purchases of investments	(1,050,598)	(17,811,395)
Maturities of investments	14,453,000	17,895,712
Purchases of fixed assets	(239,327)	(163,624)
Release of restricted cash	1,050,598	
Net cash provided by (used in) investing activities	14,213,673	(79,307)
Cash flows from financing activities:		
Proceeds from sale of stock under employee stock purchase plan	94,733	146,751
Proceeds from exercise of stock options	5,403	20,057
Payments on capital lease	(6,450)	
Net cash provided by financing activities	93,686	166,808
Net increase (decrease) in cash and cash equivalents	6,416,617	(3,131,782)
Cash and cash equivalents, beginning of period	7,097,239	7,909,778
Cash and cash equivalents, end of period	$ 13,513,856	$ 4,777,996
Supplemental disclosure of non-cash investing activities:		
Contribution of intangible asset to joint venture by Cyberkinetics	$ 2,100,000	$
Equipment acquired under capital lease		38,700

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

NeuroMetrix, Inc.

Notes to Unaudited Financial Statements

1. Business and Basis of Presentation

Business

NeuroMetrix, Inc. (the "Company"), a Delaware corporation, was founded in June 1996. The Company designs, develops and markets proprietary medical devices that aid physicians in the assessment and treatment of diseases and injuries of peripheral nerves and that provide regional anesthesia and pain control. The Company also markets a device for the evaluation of retinal disorders. The Company's primary focus to date has been on products that help physicians with the assessment of neuropathies. The Company has three products cleared by the United States Food and Drug Administration ("FDA"), including the ADVANCE System and the NC-stat System for the assessment of neuropathies and the DigiScope for the detection of eye disorders such as diabetic retinopathy. The Company initiated sales and marketing efforts for the ADVANCE System, a traditional nerve conduction and needle electromyography ("NCS/nEMG") system for the assessment of neuropathies, after receiving 510(k) clearance from the FDA in April 2008. The Company operates in one business segment.

On December 26, 2007, the Company acquired substantially all of the assets of EyeTel Imaging, Inc. ("EyeTel") for an aggregate purchase price of 1,050,297 shares of the Company's common stock valued at $9.8 million, $175,000 in cash, and $150,000 in acquisition costs for total consideration of $10.1 million. The Company also assumed certain specified liabilities totaling $804,900. EyeTel was engaged in the design, development, and commercialization of proprietary medical devices, including the DigiScope. The Company had previously entered into an exclusive licensing agreement with EyeTel pursuant to which the Company had sales and marketing rights to the DigiScope in the primary diabetes care physician market. The acquisition is intended to further diversify the Company's proprietary medical device product offering and expand sales into additional markets such as the optometry market.

In February 2008, the Company and Cyberkinetics Neurotechnology Systems, Inc., ("Cyberkinetics"), a related party, formed PNIR (Peripheral Nerve Injury Repair) LLC, ("PNIR"), a joint venture incorporated in Delaware, and entered into a Collaboration Agreement and Operating Agreement to develop and commercialize products for the treatment of peripheral nerve injury. The joint venture is initially 50% owned by the Company and 50% owned by Cyberkinetics. Under the terms of the joint venture, the Company has agreed to fund the initial $2.0 million in product development costs and the Company and Cyberkinetics have agreed to share equally in all costs in excess of the initial $2.0 million. Cyberkinetics has contributed technology, know-how and intellectual property, primarily relating to their Andara OFS (Oscillating Field Stimulator), ("Andara OFS") technology, to the joint venture.

The Company obtained sales and marketing rights and Cyberkinetics obtained commercial manufacturing rights to any products commercialized under the joint venture. Each party will charge the joint venture at cost for all expenses incurred in connection with their respective commercialization activities. Profits and losses realized from the joint venture will be split equally between the Company and Cyberkinetics based on the initial ownership percentage.

Prior to the formation of the joint venture, in November 2007, the Company made an investment of $2.5 million for the purchase of approximately 5.4 million shares of common stock of Cyberkinetics, representing approximately 13% of Cyberkinetics' issued and outstanding shares at the time of the investment, at a price of $0.46 per share. The Company also received a warrant to purchase up to approximately 2.7 million shares of Cyberkinetics common stock. The warrant is exercisable at $0.46

NeuroMetrix, Inc.

Notes to Unaudited Financial Statements (Continued)

1. Business and Basis of Presentation (Continued)

per share and has a term of five years, but will be required to be exercised if Cyberkinetics receives FDA approval of a Humanitarian Device Exemption ("HDE") filing for the Andara OFS device for acute spinal cord injuries by December 31, 2008. (See Note 2.)

The accompanying unaudited consolidated balance sheet as of June 30, 2008, unaudited statements of operations for the three and six month periods ended June 30, 2008 (consolidated) and 2007 and the unaudited statements of cash flows for the six month periods ended June 30, 2008 (consolidated) and 2007 have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by accounting principles generally accepted in the United States of America for complete financial statements. In the opinion of management, all adjustments (consisting only of normal recurring accruals) considered necessary for a fair statement of the results of operations have been included. Operating results for the three and six month periods ended June 30, 2008 are not necessarily indicative of the results that may be expected for the year ending December 31, 2008 or any other period. These financial statements and notes should be read in conjunction with the financial statements for the year ended December 31, 2007 included in the Company's Annual Report on Form 10-K (File No. 000-50856). The accompanying balance sheet as of December 31, 2007 has been derived from audited financial statements prepared at that date, but does not include all disclosures required by accounting principles generally accepted in the United States of America.

Revenue

Medical equipment revenues (formerly referred to as diagnostic device revenues) consist of sales of NC-stat devices and NC-stat docking stations and ADVANCE devices and related modules.

Consumables revenue (formerly referred to as biosensor revenues) consists of sales of single use nerve specific electrodes which are used with the NC-stat System and the ADVANCE System.

Other revenues consist entirely of revenues relating to the DigiScope.

Principles of Consolidation

The consolidated financial statements as of and for the three and six months ended June 30, 2008 reflect the Company's financial statements and those of PNIR, a joint venture with Cyberkinetics. In accordance with Financial Accounting Standards Board ("FASB") Interpretation No. 46, *Consolidation of Variable Interest Entities (revised December 2003) an interpretation of ARB No. 51*, ("FIN 46(R)"), the Company consolidates variable interest entities in which the Company is the primary beneficiary. For such consolidated entities in which the Company owns less than a 100% interest, the Company records minority interest in its consolidated statements of operations for the ownership interest of the minority owner. All material intercompany balances and transactions have been eliminated in consolidation.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at

NeuroMetrix, Inc.

Notes to Unaudited Financial Statements (Continued)

1. Business and Basis of Presentation (Continued)

the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Recent Accounting Pronouncements

In May 2008, the FASB issued Statement of Financial Accounting Standards ("SFAS") No. 162, "*The Hierarchy of Generally Accepted Accounting Principles"* ("SFAS No. 162"). SFAS No. 162 transfers the hierarchy of GAAP from the auditing literature to the accounting standards and identifies a consistent hierarchy for selecting accounting principles to be used in applying U.S. GAAP. SFAS No. 162 is effective 60 days following the SEC's approval of PCAOB Auditing Standard No. 6, "*Evaluating Consistency of Financial Statements"* ("AS/6"). The company does not expect the adoption of SFAS No. 162 to have any effect on its financial position, results of operations or cash flows.

In April 2008, the FASB issued Staff Position Statement of Financial Accounting Standards ("SFAS") No.142-3, "*Determination of the Useful Life of Intangible Assets"* ("FSP SFAS No. 142-3"). FSP SFAS No. 142-3 amends SFAS No. 142, "*Goodwill and Other Intangible Assets" (*"SFAS No. 142") to improve the consistency between the useful life of a recognized intangible asset under SFAS No. 142 and the period of expected cash flows used to measure the fair value of the asset under FASB SFAS No. 141*, "Business Combinations"* ("SFAS No. 141"), and other U.S. GAAP. FSP SFAS No. 142-3 is effective for fiscal years beginning after December 15, 2008. The guidance for determining the useful life of a recognized intangible asset is to be applied prospectively for intangibles acquired after the adoption date. Certain disclosure requirements will impact existing intangibles. The Company is currently evaluating the impact of the adoption of FSP SFAS No. 142-3.

In December 2007, the FASB issued SFAS No. 160, "*Noncontrolling Interests in Consolidated Financial Statements*" ("SFAS No. 160"). SFAS No. 160 requires that noncontrolling interests be reported as stockholders equity, a change that will affect financial statement presentation of minority interests in its consolidated subsidiaries. SFAS No. 160 also establishes a single method of accounting for changes in a parent's ownership interest in a subsidiary as long as that ownership change does not result in deconsolidation. SFAS No. 160 is required to be applied prospectively in 2009, except for the presentation and disclosure requirements which are to be applied retrospectively. SFAS No. 160 is effective for fiscal years beginning after December 15, 2008. Except for certain reclassifications required upon adoption of SFAS No. 160 and subject to change in ownership of PNIR, the joint venture, if any, the Company does not expect the adoption of SFAS No. 160 to have a material impact to its financial position, results of operations or cash flows.

In February 2007, the FASB issued SFAS No. 159, "*The Fair Value Option for Financial Assets and Financial Liabilities, including an amendment of FASB Statement No. 115*" ("SFAS No. 159"). SFAS No. 159 permits entities to choose to measure many financial instruments and certain other items at fair value that are not currently required to be measured at fair value. Unrealized gains and losses on items for which the fair value option has been elected are reported in earnings. SFAS No. 159 does not affect any existing accounting literature that requires certain assets and liabilities to be carried at fair value. SFAS No. 159 is effective for fiscal years beginning after November 15, 2007. The Company did not elect to measure at fair value any additional assets or liabilities that are not already measured at fair value under existing standards. The adoption of SFAS No. 159 did not have a material impact on its financial position, results of operations or cash flows.

NeuroMetrix, Inc.

Notes to Unaudited Financial Statements (Continued)

1. Business and Basis of Presentation (Continued)

In September 2006, the FASB issued SFAS No. 157, *"Fair Value Measurements"* ("SFAS No. 157"). SFAS No. 157 defines fair value in numerous accounting pronouncements, establishes a framework for measuring fair value in generally accepted accounting principles ("GAAP") and expands disclosures related to the use of fair value measures in financial statements. SFAS No. 157 does not expand the use of fair value measures in financial statements, but standardizes its definition and guidance in GAAP. SFAS No. 157 emphasizes that fair value is a market-based measurement and not an entity-specific measurement based on an exchange transaction in which the entity sells an asset or transfers a liability (exit price). SFAS No. 157 establishes a fair value hierarchy from observable market data as the highest level to fair value based on an entity's own fair value assumptions as the lowest level. SFAS No. 157 is effective for assets and liabilities as of January 1, 2008. In February 2008, the FASB issued FASB Statement of Position, ("FSP") No. 157-2 "*Partial Deferral of the Effective Date of Statement 157,*" ("FSP No. 157-2"), which delays the effective date of SFAS No. 157 for all non-financial assets and non-financial liabilities, except those that are recognized or disclosed at fair value in the financials statements on a recurring basis (at least annually) to fiscal years beginning after November 15, 2008. The adoption of SFAS No. 157 did not have a material effect on the Company's financial position, results of operations or its cash flows. (See Note 10.)

2. Comprehensive Loss

SFAS No. 130, "*Reporting Comprehensive Income*" establishes standards for reporting and displaying comprehensive income and its components in a full set of general-purpose financial statements. In November 2007, the Company made an investment of $2.5 million in shares and warrants for Cyberkinetics common stock and is accounting for this investment as an available-for-sale security under the provisions of SFAS No. 115, *"Accounting for Certain Investments in Debt and Equity Securities"*. At December 31, 2007, the Company recorded $1.4 million as a temporary impairment within other comprehensive income. For the three and six months ended June 30, 2008, the Company reassessed its investment in Cyberkinetics and based on the outlook for Cyberkinetics and the period of the time that the common stock of Cyberkinetics has traded below the price paid by the Company for its investment, has recognized losses of $1.4 million and $2.1 million, respectively, due to an impairment in the value of the investment that the Company determined was other-than-temporary.

	Three Months Ended		Six Months Ended	
	June 30, 2008	June 30, 2007	June 30, 2008	June 30, 2007
	(Consolidated)		(Consolidated)	
Comprehensive loss:				
Net loss	$(4,927,938)	$(1,290,991)	$(15,735,455)	$(2,668,273)
Other comprehensive income:				
Reclassification adjustment for recognized loss included in net earnings			1,441,745	
Other comprehensive income			1,441,745	
Comprehensive loss	$(4,927,938)	$(1,290,991)	$(14,293,710)	$(2,668,273)

The Company may be required to record future losses on its Cyberkinetics investment if there is not an improvement in the Cyberkinetics outlook or if their common stock price declines further. At June 30, 2008, the Company's investment in Cyberkinetics was $442,835.

NeuroMetrix, Inc.

Notes to Unaudited Financial Statements (Continued)

3. Net Loss Per Common Share

The Company accounts for and discloses net loss per common share in accordance with SFAS No. 128, "*Earnings Per Share*". Basic net loss per common share is computed by dividing net loss by the weighted average number of common shares outstanding. Diluted net loss per common share is computed by dividing net loss by the weighted average number of common shares and dilutive potential common share equivalents then outstanding. Potential common shares consist of shares issuable upon the exercise of stock options (using the treasury stock method.)

The following potentially dilutive common shares were excluded from the calculation of diluted net loss per common share because their effect was antidilutive for each of the periods presented:

	Three Months Ended		Six Months Ended	
	June 30, 2008	June 30, 2007	June 30, 2008	June 30, 2007
Options outstanding	2,477,436	1,794,029	2,477,436	1,794,029

4. Inventories

Inventories consist of the following:

	June 30, 2008	December 31, 2007
Purchased components	$1,412,103	$ 1,216,758
Finished goods	4,733,187	4,137,580
	$6,145,290	$ 5,354,338

5. Acquisition

On December 26, 2007, the Company acquired substantially all of the assets of EyeTel for an aggregate purchase price of 1,050,297 shares of the Company's common stock valued at $9.8 million, $175,000 in cash, and $150,000 in acquisition costs for a total consideration of $10.1 million. The Company also assumed certain specified liabilities totaling $804,900. EyeTel was engaged in the design, development, and commercialization of proprietary medical devices, including the DigiScope, a device that helps physicians detect eye disorders such as diabetic retinopathy, the leading cause of blindness in patients with diabetes. The Company had previously entered into an exclusive licensing agreement with EyeTel pursuant to which the Company had sales and marketing rights to the DigiScope in the primary diabetes care physician market. The acquisition is intended to further diversify the Company's proprietary medical equipment product offering and expand sales into additional markets such as the optometry market.

Pro Forma Financial Summary (Unaudited)

The following pro forma financial summary is presented as if the acquisition of EyeTel was completed as of the beginning of 2007. The pro forma combined results are not necessarily indicative

NeuroMetrix, Inc.

Notes to Unaudited Financial Statements (Continued)

5. Acquisition (Continued)

of the actual results that would have occurred had the acquisition been consummated on that date, or of the future operations of the combined entities.

	Pro Forma Results	
	Three Months Ended June 30, 2007	Six Months Ended June 30, 2007
Total revenues	$ 11,541,623	$ 23,367,972
Net loss	$ (3,465,375)	$ (6,846,609)
Net loss per common share (basic and diluted):	$ (0.25)	$ (0.50)
Weighted average shares used to compute net loss per common share (basic and diluted):	13,662,177	13,658,970

6. Goodwill and Intangible Assets

Goodwill

As a result of the acquisition of substantially all of the assets of EyeTel on December 26, 2007, the Company recorded approximately $5.8 million of goodwill on its balance sheet at December 31, 2007. In accordance with the provisions of SFAS No. 142, "*Goodwill and Other Intangible Assets*" ("SFAS No. 142"), the Company is required to assess the realizability of goodwill annually, and whenever events or changes in circumstances suggest that the carrying amount may not be recoverable. The operations of EyeTel were incorporated into the Company's one segment and the Company determined that it is comprised of a single reporting unit for goodwill impairment testing. Subsequent to the American Medical Association ("AMA") CPT Editorial Panel ("CPT Panel") meeting in February 2008, the Company's common stock price declined significantly such that as of March 31, 2008, the Company's publicly traded market value was below its net book value. Based on this, the Company determined that an interim goodwill impairment test was required. As the net book value of the Company's assets exceeded the enterprise value, the Company performed step two of its SFAS No. 142 impairment test in which it assessed the fair value of all recorded and unrecorded tangible and intangible assets and liabilities, including its recently acquired EyeTel and PNIR intangible assets. The Company determined that no assets were impaired and determined that there was no residual value of goodwill. Accordingly, the Company recorded a charge of $5.8 million to write off the goodwill balance during the three months ended March 31, 2008.

Intangible Assets

Intangible assets at June 30, 2008 and December 31, 2007 were $4.5 million and $2.8 million, respectively. As of June 30, 2008, intangible assets included $2.8 million of gross intangible assets representing the fair value of technology and intellectual property resulting from the Company's December 26, 2007 acquisition of substantially all of the assets of EyeTel and $2.1 million of gross intangible assets representing the value of the contribution of technology and intellectual property by Cyberkinetics upon the formation of PNIR. (See Note 1.) Accumulated amortization of intangible assets at June 30, 2008 and December 31, 2007 was $437,500 and $0, respectively. Amortization expense for the three and six months ended June 30, 2008 was $245,000 and $437,500, respectively. There was no amortization expense for the same periods a year ago.

NeuroMetrix, Inc.

Notes to Unaudited Financial Statements (Continued)

6. Goodwill and Intangible Assets (Continued)

The Company amortizes its intangible assets using the straight-line method over their estimated economic lives, which is estimated to be five years.

The estimated future amortization expense for intangible assets for the remainder of 2008, the four succeeding fiscal years and thereafter is as follows:

	Estimated Amortization
2008 (remaining six months)	$ 490,000
2009	980,000
2010	980,000
2011	980,000
2012	980,000
Thereafter	52,500

The recoverability of the Company's intangible assets is dependent upon its ability to successfully market the DigiScope and to successfully develop marketable products from PNIR, its joint venture with Cyberkinetics. If there are events or conditions that suggest the Company's ability to recover the carrying value of these or other long lived assets is in doubt, the Company will be required to perform future impairment tests of long lived assets under SFAS No. 144 "*Accounting for the Impairment or Disposal of Long-Lived Assets*". Impairment charges, if any, could be material to the Company's results of operations and financial condition.

7. Long-Term Available-For-Sale Investment

In November 2007, the Company made an investment of $2.5 million for the purchase of approximately 5.4 million shares of common stock of Cyberkinetics, representing approximately 13% of Cyberkinetics' issued and outstanding shares at the time of the investment, at a price of $0.46 per share. The Company also received a warrant to purchase up to approximately 2.7 million shares of Cyberkinetics common stock. The warrant is exercisable at $0.46 per share and has a term of five years, but will be required to be exercised if Cyberkinetics receives FDA approval of an HDE filing for the Andara OFS device for acute spinal cord injuries by December 31, 2008.

The Company accounts for the investment in Cyberkinetics as an available-for-sale investment and reviews the carrying value of this investment quarterly to determine whether an other-than-temporary decline in market value exists. The Company marked this investment to market for the three and six months ended June 30, 2008 and recognized losses of $1.4 million and $2.1 million, respectively, because the decline in the value of this investment was considered other-than-temporary. The Company considered factors such as the length of time the value of the investment has been below its original purchase price, the financial condition of the investee and near-term prospects for the investee's recovery to original purchase price and the Company's intent with regard to the underlying investment. The Company may record future losses on its Cyberkinetics investment if there is not an improvement in the Cyberkinetics outlook or if the market value of their common stock declines further.

NeuroMetrix, Inc.

Notes to Unaudited Financial Statements (Continued)

8. Other Balance Sheet Items

Other accrued expenses consist of the following:

	June 30, 2008	December 31, 2007
Professional services	$ 793,717	$ 706,952
Sales taxes	374,802	489,555
Other	1,050,884	1,112,056
	$2,219,403	$ 2,308,563

Product Warranty Costs

The Company accrues estimated product warranty costs at the time of sale which are included in cost of sales in the statements of operations. The amount of the accrued warranty liability is based on historical information such as past experience, product failure rates, number of units repaired and estimated cost of material and labor. The liability for product warranty costs is included in accrued expenses in the balance sheet.

The following is a rollforward of the Company's accrued warranty liability for the three and six month periods ended June 30, 2008 and 2007:

	Three Months Ended		Six Months Ended	
	June 30, 2008	June 30, 2007	June 30, 2008	June 30, 2007
Balance at beginning of period	$ 252,466	$ 252,258	$ 251,948	$ 231,725
Accrual for warranties	152,217	211,688	333,260	396,976
Settlements made	(173,391)	(183,743)	(353,916)	(348,498)
Balance at end of period	$ 231,292	$ 280,203	$ 231,292	$ 280,203

9. Joint Venture with Cyberkinetics

In February 2008, the Company and Cyberkinetics formed PNIR and entered into a Collaboration Agreement and Operating Agreement to develop and commercialize products for the treatment of peripheral nerve injury. The joint venture is initially 50% owned by the Company and 50% owned by Cyberkinetics. Under the terms of the joint venture, the Company has agreed to fund the initial $2.0 million in product development costs and the Company and Cyberkinetics will share equally in all costs in excess of the initial $2.0 million. Cyberkinetics has contributed technology, know-how and intellectual property, primarily relating to their Andara OFS technology, to the joint venture.

The Company obtained sales and marketing rights and Cyberkinetics obtained commercial manufacturing rights to any products commercialized under the joint venture. Each party will charge the joint venture at cost for all expenses incurred in connection with their respective commercialization activities. Profits and losses realized from the joint venture will be split equally between the Company and Cyberkinetics based on the initial ownership percentage.

The joint venture is considered to be a variable interest entity under the provisions of FIN 46(R). The Company has determined that it is the primary beneficiary based on a review of the relative economic risks of the two parties to the joint venture. As a result, the Company has consolidated the

NeuroMetrix, Inc.

Notes to Unaudited Financial Statements (Continued)

9. Joint Venture with Cyberkinetics (Continued)

joint venture and recorded the $2.1 million contribution of technology and intellectual property by Cyberkinetics to intangible assets and a minority interest of $2.1 million at the formation date of the joint venture. The fair value of the intangible assets was determined primarily by an assessment made by the Company's management applying the income approach and a relief from royalty approach.

Cyberkinetics, in its Form 10-Q filed on May 15, 2008, disclosed that if, before the end of September 2008, it has not been successful in raising additional capital and it has not received approval from the FDA of its HDE filing for the Andara OFS device for acute spinal cord injuries, thereby triggering the required exercise of the warrant held by us, it may be required to cease operations or seek bankruptcy protection. If Cyberkinetics is required to cease operations or seek bankruptcy protection, or if other adverse developments relating to its business or financial condition occur, the value of our investment in, and our joint venture with, Cyberkinetics could be adversely affected.

10. Commitments and Contingencies

Cyberkinetics

In connection with the Company's investment in Cyberkinetics, the Company received a warrant to purchase up to approximately 2.7 million shares of Cyberkinetics common stock. The warrant, exercisable at $0.46 per share, or approximately $1.25 million, has a term of five years, and is required to be exercised if Cyberkinetics receives FDA approval of an HDE filing for the Andara OFS device for acute spinal cord injuries by December 31, 2008.

In February 2008, the Company entered into a Collaboration Agreement and Operating Agreement with Cyberkinetics and formed PNIR, a joint venture to develop and commercialize products for the treatment of peripheral nerve injury. Under the terms of the joint venture, the Company has agreed to fund the initial $2.0 million in product development costs and has agreed to share equally in all costs in excess of the initial $2.0 million. As of June 30, 2008, there have been no expenses or cash funding in connection with PNIR other than amortization of the intangible asset.

Operating Lease

In February 2008, the Company amended the Lease Agreement dated October 18, 2000 between Fourth Avenue LLC and the Company for office and engineering laboratory space. The amendment extends the term of the lease, previously scheduled to expire on March 31, 2009, through March 31, 2013. Base rent for the period April 2009 through March 2013 will be reduced from the current level of $930,000 annually to a range of $675,000 to $765,000 annually. This amendment also provides the Company reimbursement from Fourth Avenue LLC for certain improvements and renovations to the facility up to a maximum of $240,000.

In connection with the amendment of the lease, the amount of the irrevocable letter of credit required to be maintained by the Company for the benefit of the lessor was reduced from $1,430,000 to $400,000. The letter of credit must be secured by a certificate of deposit in an amount equal to 102% of the letter of credit as security.

NeuroMetrix, Inc.

Notes to Unaudited Financial Statements (Continued)

10. Commitments and Contingencies (Continued)

Future minimum lease payments under noncancelable operating leases as of June 30, 2008 are as follows:

2008 (remaining six months)	$ 465,000
2009	738,750
2010	697,500
2011	727,500
2012	757,500
thereafter	191,250
Total minimum lease payments	$3,577,500

11. Fair Value Measurements

The Company adopted SFAS No. 157 effective January 1, 2008 for its financial assets and liabilities that are re-measured and reported at fair value at each reporting period. In accordance with the provisions of FSP No. 157-2, the Company elected to defer implementation of SFAS No. 157 as it related to its non-financial assets and liabilities that are recognized and disclosed at fair value in the financial statements on a non-recurring basis until January 1, 2009. The Company is evaluating the impact, if any, that SFAS No. 157 will have on our non-financial assets and liabilities.

The adoption of SFAS No. 157 with respect to financial assets and liabilities and non-financial assets and liabilities that are re-measured and reported at fair value at least annually was not material to the Company's financial position, results of operations or its cash flows for the period ended June 30, 2008. SFAS No. 157 defines fair value, establishes a framework for measuring fair value in applying generally accepted accounting principles, and expands disclosures about fair value measurements. SFAS No. 157 identifies two kinds of inputs that are used to determine the fair value of assets and liabilities: observable and unobservable. Observable inputs are based on market data or independent sources while unobservable inputs are based on the company's own market assumptions. Once inputs have been characterized, SFAS No. 157 requires companies to prioritize the inputs used to measure fair value into one of three broad levels. Fair values determined by Level 1 inputs utilized quoted prices (unadjusted) in active markets for identical assets or liabilities. Fair values identified by Level 2 inputs utilize observable inputs other than level 1 prices, such as quoted prices for similar assets or liabilities, quoted prices in markets that are not active or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the related assets or liabilities. Fair values identified by Level 3 inputs are unobservable data points and are used to measure fair value to the extent that observable inputs are not available. Unobservable inputs reflect the Company's own assumptions about the assumptions that market participants would use at pricing the asset or liability.

NeuroMetrix, Inc.

Notes to Unaudited Financial Statements (Continued)

11. Fair Value Measurements (Continued)

The following table provides fair value measurement information for the Company's major categories of financial assets and liabilities measured on a recurring basis:

		Fair Value Measurements at Reporting Date Using		
	June 30, 2008	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets:				
Cash equivalents	$12,344,065	$ 12,344,065	$	$
Long-term available-for-sale investment	442,835	442,835		
Total	$12,786,900	$ 12,786,900	$	$

As of June 30, 2008, the Company's long-term investment consisted of an investment in Cyberkinetics, a publicly traded security whose fair value is readily determinable.

12. Legal Matters

In March and April 2008, a series of putative securities class action and shareholder derivative lawsuits were filed against the Company and certain of its current and former executive officers and directors alleging, among other things, that the Company violated the federal securities laws and other laws by allegedly making material false and misleading statements for various periods from August 2004 through the dates the lawsuits were filed and by allegedly failing to disclose material information to the investing public. The Company believes that the claims in the cases are without merit and will vigorously contest these lawsuits.

In the second quarter of 2006, the Company received a subpoena from the Office of Inspector General ("OIG") of the Department of Health and Human Services requesting documents in connection with an investigation of potential violations of the federal anti-kickback statute and False Claims Act. In addition, on June 21, 2007, the Company received a subpoena from the U.S. Attorney's Office for the District of Massachusetts requesting documents in connection with an investigation by the United States Department of Justice ("DOJ"). The DOJ is investigating various aspects of the Company's practices relating to the NC-stat System, including sales and marketing practices. The Company is cooperating with both investigations. During 2007, the Company formed a Special Committee of its Board of Directors to provide oversight of an ongoing independent review of the Company's sales and marketing practices and of the Company's continuing cooperation with the DOJ and OIG investigations. The Company cannot predict the ultimate outcome of these investigations. The Company is unable to determine when these matters will be resolved, whether any additional areas of inquiry will be opened, or any outcome of this matter and accordingly these financial statements do not include any amounts related to the outcome of this matter. Any negative findings in this matter could result in fines, penalties, or program exclusions, which could have a material adverse effect on the Company's financial condition, results of operations, and cash flows.

NeuroMetrix, Inc.

Notes to Unaudited Financial Statements (Continued)

13. Restructuring Related Activity

In May 2008, the Company implemented a plan to reduce the size of its direct sales force and to take certain other actions to reduce its operating expenses, largely as a result of a decline in revenues. These actions affected 24 positions, substantially all of which were in sales. The total cost associated with these actions, including severance and benefit costs, was $318,981.

Effective May 31, 2008, the Chief Operating Officer of the Company entered into a separation agreement with the Company. Under the terms of the separation agreement, he will receive continuation of his salary, car allowance and health benefits for nine months following the effectiveness of his resignation, equal to $217,970, which we recorded during the quarter ended March 31, 2008 under the provisions of SFAS No. 112 *"Employers Accounting for Postemployment Benefits an amendment of FAS Statements No. 5 and 43."* In addition, he received a lump sum payment equal to three months salary and car allowance totaling $69,810, which we recorded during the quarter ended June 30, 2008 under the provisions of SFAS No. 146, "*Accounting for Costs Associated with Exit or Disposal Activities."*

The following table provides a rollforward of the current liability balance for the action taken, substantially all of which was recorded as sales and marketing expense on the Company's Consolidated Statement of Operations, the balance of which will be paid out in semi-monthly installments through February 28, 2009.

	Three Months Ended June 30, 2008	Six Months Ended June 30, 2008
Balance at beginning of period	$ 217,970	$
Accrual for severance	388,791	606,761
Payments made	(377,140)	(377,140)
Balance at end of period	$ 229,621	$ 229,621

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

You should read the following discussion of our financial condition and results of operations in conjunction with our financial statements and the accompanying notes to those financial statements included elsewhere in this Quarterly Report on Form 10-Q. This discussion contains forward-looking statements that involve risks and uncertainties. For a description of factors that may cause our actual results to differ materially from those anticipated in these forward looking statements, please refer to the section of this Quarterly Report on Form 10-Q titled "Cautionary Note Regarding Forward-Looking Statements." Unless the content otherwise requires, all references to "we", "us", "the Company" or "NeuroMetrix" in this Quarterly Report on Form 10-Q refers to NeuroMetrix, Inc. and its consolidated entities unless the content requires otherwise.

Overview

NeuroMetrix was founded in June 1996. We design, develop and market proprietary medical devices that aid physicians in the assessment and treatment of diseases and injuries of peripheral nerves and that provide regional anesthesia and pain control. We also market a device for the evaluation of retinal disorders. Our focus to date has been on products that help physicians with the assessment of neuropathies and neurovascular conditions. We have three products cleared by the United States Food and Drug Administration, or FDA, including the ADVANCE System and the NC-stat System for the assessment of neuropathies and the DigiScope for the detection of eye disorders such as diabetic retinopathy. We initiated our sales and marketing efforts in May 2008 for the ADVANCE System, a traditional nerve conduction and needle electromyography, or NCS/nEMG, system for the assessment of neuropathies, which received 510(k) clearance from the FDA in April 2008.

We believe that our neuropathy assessment systems can improve the quality and efficiency of patient care by offering physicians the ability to objectively assess patients with neuropathies, resulting in earlier and more accurate detection, and, potentially improved clinical outcomes. We are presently focusing our medical equipment sales efforts primarily on the ADVANCE System and we are marketing this system primarily to specialist physicians with peripheral nerve expertise, including neurologists, physical medicine and rehabilitation physicians, neurosurgeons, orthopedic and hand surgeons and pain medicine physicians. The ADVANCE System is a system for the performance of traditional nerve conduction studies and needle electromyography procedures. The ADVANCE System is comprised of: (1) single use surface electrodes (currently limited to our nerve specific electrodes which are also used with the NC-stat System) and needles, (2) the ADVANCE device and related modules, and (3) a communication hub that enables the physician's office to network their device to our onCall Information System for data archiving, report generation and other network services.

The NC-stat System, our first product for the assessment of neuropathies, has been sold historically to a broad group of physicians, including primary care physicians and specialists since its initial market launch in May 1999 and is used in over 5,400 physician's offices and clinics in the United States. Over 1.0 million patients have had nerve conduction tests performed using the NC-stat System. Substantially all of our revenues to date have been derived from sales of the NC-stat System. Due to reimbursement uncertainty described in further detail below, we are presently focusing our medical equipment sales efforts primarily on sales of the ADVANCE System to specialist physicians with peripheral nerve expertise. We continue to sell electrodes to and support our NC-stat customer base, work with our existing NC-stat customers in specialty practices to convert them to the ADVANCE System and provide solutions that enable our customers to provide this important diagnostic service to their patients.

Acquisition

In December 2007, we acquired substantially all of the assets of EyeTel Imaging, Inc., or EyeTel, and their product, the DigiScope, a product used for the detection of eye disorders such as diabetic retinopathy, an eye disease prevalent in patients with diabetes. The DigiScope is marketed to the primary diabetes care physician office market and the optometry market. Prior to the acquisition of substantially all of the assets of EyeTel, we had been marketing the DigiScope to the primary diabetes care physician office market through an exclusive sales and marketing license with EyeTel. The DigiScope allows physicians to detect diabetic retinopathy and refer patients to an eye specialist for treatment if deemed necessary based on the results. It is recommended by the American Diabetes Association, or ADA, that all patients with diabetes receive an annual dilated eye examination to monitor vision. According to the ADA, there are approximately 21.0 million people in the United States with diabetes and only approximately 50% comply with the recommendation to have an annual eye examination. We believe that a product such as the DigiScope could potentially lead to an increase in the level of testing and result in the earlier detection of eye diseases in patients with diabetes and potentially improved clinical outcomes.

Corporate Collaborations

In November 2007, we made an investment of $2.5 million for the purchase of approximately 5.4 million shares of common stock of Cyberkinetics Neurotechnology Systems, Inc., or Cyberkinetics. We also received a warrant to purchase up to approximately 2.7 million shares of Cyberkinetics common stock. The warrant will be required to be exercised if Cyberkinetics receives FDA approval of a Humanitarian Device Exemption, or HDE, filing for the Andara Oscillating Field Stimulator , or Andara OFS, device for acute spinal cord injuries by December 31, 2008. In connection with the investment in Cyberkinetics, we also received certain rights, including a right of first negotiation for the acquisition of Cyberkinetics and a right of first negotiation for the commercialization of the Andara OFS device for the treatment of acute spinal cord injuries. This right of first negotiation for the acquisition of Cyberkinetics has expired.

In February 2008, we entered into a Collaboration Agreement and Operating Agreement with Cyberkinetics to develop and commercialize products for the treatment of peripheral nerve injury and formed PNIR (Peripheral Nerve Injury Repair) LLC, or PNIR, a joint venture with 50% ownership held by us and 50% ownership held by Cyberkinetics.

Business Developments

Historically, we have derived substantially all of our revenues from the sales of the NC-stat System, including the sale of medical equipment and consumables, which we also refer to as nerve specific electrodes, previously referred to as biosensors. During the second quarter of 2008, we recognized our initial revenues from sales of the ADVANCE System to specialist physicians with peripheral nerve expertise. We also derive revenues from sales of the DigiScope to physician groups and optometry clinics.

Our revenues declined to $8.5 million for the three months ended June 30, 2008, compared to $11.5 million for the same period in 2007. Additionally, we incurred a net loss of $4.9 million for the three months ended June 30, 2008, compared to a net loss of $1.3 million for the same period in 2007. We believe that the decline in our revenues has been caused primarily by the current environment relating to the reimbursement by third-party payers of nerve conduction studies performed using the NC-stat System and we expect that our revenues from sales of the NC-stat System may continue to be adversely affected by the uncertainty regarding reimbursement.

Significant developments impacting and relating to our financial condition and results of operations as of and for the three and six months ended June 30, 2008 and expected to impact future periods, include:

Reimbursement developments relating to nerve conduction studies on our revenues as described below, including the outcome of the AMA CPT Editorial Panel review of reimbursement coding for nerve conduction studies performed using equipment such as the NC-stat System and the material and adverse impact the potential issuance of a Category III CPT code by the AMA CPT Editorial Panel is likely to have on our revenues and operating results.

The recent launch of the ADVANCE System, a system for the performance of traditional nerve conduction studies and needle electromyography procedures, which occurred in May 2008 following the 510(k) clearance by the FDA. We are primarily focusing our sales and marketing efforts for the ADVANCE System on specialist physicians with peripheral nerve expertise, including neurologists, physical medicine and rehabilitation physicians, neurosurgeons, orthopedic and hand surgeons and pain medicine physicians in the United States.

Sales and marketing efforts for the DigiScope as a result of the acquisition of substantially all of the assets of EyeTel and with the launch into the optometry market. We are currently evaluating the level of sales and marketing effort and the development effort we plan to allocate to the DigiScope.

The reduction in the size of the sales force from 50 regional sales managers to 30 regional sales managers and certain other cost reduction steps taken during the second quarter of 2008. These steps were taken largely as a result of a decline in revenues we have experienced. We expect that our operating expenses will be reduced by approximately $5.0 million on an annualized basis, as a result of these actions, compared to operating expense levels prior to these actions being taken. Our sales and marketing expenses declined by approximately $1.6 million during the second quarter of 2008 as compared to the first quarter of 2008 primarily due to this cost reduction program.

Our decision to terminate the relationships with our independent sales agencies in the second half of 2007, which we believe has adversely impacted our revenues, but has resulted in the elimination of commissions on recurring revenues from accounts originally sourced through our independent sales agencies. Total commissions relating to independent sales agencies were $0 and $833,500 for the three months ended June 30, 2008 and 2007, respectively.

The government investigations by the Office of Inspector General, or OIG, of the Department of Health and Human Services and the U.S. Department of Justice, or DOJ, that we are subject to, which resulted in significantly increased legal expenses in 2007 and in the first six months of 2008. We cannot predict the potential impact of these investigations on our financial condition or financial results in 2008.

Continued progress developing a product designed to precisely deliver pharmacologic agents such as anesthetics and corticosteroids in close proximity to nerves for regional anesthesia, pain control and the treatment of focal neuropathies such as carpal tunnel syndrome for which we plan to file one or more 510(k) applications with the FDA in the second half of 2008. We continue to invest resources on the development of this product.

The investment we made in Cyberkinetics in the fourth quarter of 2007, which included the purchase of $2.5 million of Cyberkinetics common stock and the receipt of a warrant to purchase an additional $1.25 million of Cyberkinetics common stock that we must exercise in certain circumstances. The value of this investment has declined substantially and we believe that this decline is not temporary in nature, and have therefore taken a charge to earnings for the decline in value through June 30, 2008. We entered into a joint venture with Cyberkinetics for

the development of a treatment for peripheral nerve injury, for which we have committed to fund the first $2.0 million in development expenses and 50% of any development costs exceeding the initial $2.0 million.

Reimbursement from third-party payers is an important element of success for medical device companies. As our presence in the market over the last several years has expanded with the use of the NC-stat System, physicians using NC-stat have experienced and are likely to continue to experience an increased focus from third-party payers and governmental agencies regarding the reimbursement of nerve conduction studies performed using this device and an increased focus from these organizations regarding the professional requirements for performing nerve conduction studies in general. A number of third-party payers, including commercial payers, have taken and may continue to take the position of not reimbursing our customers for procedures performed using the NC-stat System.

During the second half of 2006 and in 2007, several local Medicare carriers issued draft local coverage determinations, or LCDs, final LCDs or coding articles particularly addressing coverage and reimbursement policies under Medicare for nerve conduction studies performed using the NC-stat System. Several of these carriers indicated that they will not reimburse physicians under Medicare for nerve conduction studies performed using the NC-stat System under the three existing Current Procedural Terminology, or CPT, codes for conventional nerve conduction studies (95900, 95903 and 95904), which provide for levels of reimbursement fixed by the Center for Medicaid and Medicare Services but rather that physicians must submit claims for reimbursement for these procedures under a miscellaneous CPT code (95999), in which case the local carriers may determine the level of reimbursement to be paid, if any. Currently, there are four local Medicare carriers with final LCDs which address coverage and reimbursement policies under Medicare for nerve conduction studies performed using the NC-stat System. In certain regions impacted by these reimbursement decisions, our customers have experienced lower levels of reimbursement and higher levels of claims denials. If physicians do not receive adequate reimbursement under the miscellaneous CPT code from those local carriers, our existing customers may continue to limit or curtail their use of the NC-stat System and we may be unable to obtain new customers, both of which could materially and adversely impact our revenues and profitability.

The AMA formed a work group in early 2007 to examine the reimbursement coding of nerve conduction studies performed using nerve conduction equipment, including the NC-stat System. The findings of this work group were presented to the AMA CPT Panel at a meeting in February 2008. During the CPT Panel meeting, several proposals for new Category I CPT codes, which generally are included in the Medicare physician fee schedule and are assigned specified reimbursement values, were presented by the chairpersons of the work group and were supported by several physician societies. Although the AMA voted on a Category III code describing nerve conduction studies performed with pre-configured electrodes at its February 2008 meeting, the AMA did not publish any new Category III CPT codes for nerve conduction studies on July 1, 2008 when it published its list of new Category III CPT codes. However, the AMA could still publish a Category III code for nerve conduction studies performed using procedures such as with the NC-stat System at a later date. In the event that a Category III CPT code is published which describes nerve conduction studies performed with the NC-stat System, it would likely result in limited Medicare reimbursement for such studies as a result of the potential that no specified reimbursement values would be assigned to these codes. This will likely adversely impact reimbursement by other third party payers and will likely have an adverse and material impact on our revenues and results of operations.

The LCDs and coding articles issued by local Medicare carriers have also addressed a number of other issues, including (1) the background and training of physicians supervising or performing nerve conduction studies, (2) the level of training requirements for technicians performing a nerve conduction study, (3) whether nerve conduction tests should be required to be performed concomitantly with a needle electromyography procedure and (4) whether the NC-stat System is comparable to conventional

nerve conduction testing equipment. We do not believe that these LCDs prohibit physicians from receiving reimbursement under Medicare for medically necessary nerve conduction studies performed using the NC-stat System. However, these LCDs do appear to be targeted at limiting access to perform and/or reimbursement for nerve conduction studies. In certain cases, these LCDs are being interpreted or implemented in a manner that impacts the ability of physicians to receive reimbursement under Medicare, including lower levels of reimbursement and an increase in the number of claims being denied, for nerve conduction studies performed using the NC-stat System, which are having an adverse impact on our revenues.

Additionally, a significant number of commercial payers, including the majority of regional Blue Cross Blue Shield carriers, and other major private payers, have adopted policies indicating that they will not provide reimbursement for the use of the NC-stat System. These commercial payers have cited various reasons for their reimbursement policies, including, among others, that the NC-stat System is experimental and investigational. We are in the process of communicating with these payers directly, through our customers or through our network of reimbursement consultants, to attempt to address their concerns. Third-party payers may also impose requirements on physicians to submit additional paperwork supporting the medical necessity of nerve conduction studies performed using the NC-stat System. We believe these requirements are negatively impacting the use of the NC-stat System by existing customers and our sales to new customers, both of which are having an adverse impact on our revenues.

Additional third-party payers, including local Medicare carriers and commercial payers, could potentially take a position that could reduce or eliminate the reimbursement for nerve conduction studies performed with the NC-stat System and could have the impact of deterring usage by our customers which could have an adverse impact on our revenues.

In the second quarter of 2008, we received 510(k) clearance from the FDA for the marketing in the United States of the ADVANCE System, a system for the performance of traditional nerve conduction studies and needle electromyography procedures. The ADVANCE System was cleared by the FDA with the primary predicate, or comparable, device being the Keypoint device originally manufactured and marketed by Medtronic, Inc. to neurologists and physical medicine and rehabilitation physicians for the performance of nerve conduction studies and needle electromyography procedures. The ADVANCE System is a traditional system that supports nerve conduction testing with any electrode methodology, real-time waveform review and cursor editing, needle electromyography procedures and conventional reports with the results of the testing. We launched our sales and marketing efforts for the ADVANCE System to specialists with peripheral nerve expertise such as neurologists, physical medicine and rehabilitation physicians, neurosurgeons, orthopedic and hand surgeons and pain medicine physicians in May 2008. Our success in selling the ADVANCE System will be dependent, among other things, on our customers' receiving, and our potential customers' belief that they will receive, sufficient reimbursement from third-party payers for performing procedures using the ADVANCE System. We do not believe that the final LCDs or policies adopted by major private payers impacting reimbursement for procedures performed using the NC-stat System will apply to procedures performed by specialists with peripheral nerve expertise using the ADVANCE System. However, these final LCDs and policies are subject to the interpretation of, and may be modified by, the applicable third-party payer, whose interpretations may differ from ours. Additionally, the outcome of the ongoing process with the AMA CPT Panel regarding reimbursement coding of nerve conduction studies could impact future reimbursement of procedures performed using the ADVANCE System.

We believe that eye scans performed using the DigiScope are being reimbursed by the majority of third-party payers. Many commercial payers have policies in place providing for reimbursement for the use of the DigiScope and many of these payers have published favorable articles about the DigiScope in their newsletters. However, several Medicare carriers have issued draft LCDs and coding articles that require a diagnosis of pre-existing retinal disease and/or will only reimburse for fundus photography, a

highly specialized form of medical imaging, when performed in conjunction with an eye examination performed by an eye specialist. There are no assurances that other Medicare carriers will not issue similar draft LCDs, final LCDs or coding articles restricting the reimbursement for the use of the DigiScope. We believe that eye examinations performed on patients covered by Medicare represented less than 25% of our DigiScope revenues in 2007. However, the restrictions on reimbursement by Medicare carriers could have an adverse impact on our ability to grow our DigiScope revenues in future periods. We have also launched the DigiScope into the optometry market and tests performed by optometrists may include screens that are paid for out of pocket by patients and full medical tests which are submitted to third-party payers for reimbursement.

 th="1%"> For revenues derived from insurance payers, pharmacies and submitters, such revenues are recognized on a per transaction basis or flat fee basis in the period the services are rendered. Revenue from our medical cost containment business is recognized when the services are performed and are recorded net of estimated allowances. These revenues are primarily in the form of fees generated from discounts we secure for payers that access our provider network. Revenues associated with revenue sharing agreements are recorded as gross revenue on a per transaction basis or a percentage of revenue basis and may involve increasing amounts or percentages based on transaction or revenue volumes achieved. This treatment is in accordance with Emerging Issues Task Force Consensus No. 99-19, Reporting Revenue Gross as a Principal Versus Net as an Agent. Revenue from certain up-front fees is recognized ratably over three years, which is the expected life of the customer. This treatment is in accordance with Staff Accounting Bulletin No. 104, Revenue Recognition (SAB No. 104). Revenue from support and maintenance contracts is recognized ratably over the contract period.

Revenues in the Company s Laboratory Communication Solutions segment are recorded as follows:

Revenue from support and maintenance contracts is recognized ratably over the contract period.

Revenues from the sale of inventory and manufactured goods is recognized when the product is delivered, price is fixed or determinable, and collectibility is probable. This treatment is in accordance with SAB No. 104.

Table of Contents

Revenue from the rental of laboratory communication devices is recognized ratably over the period of the rental contract.

Goodwill We adopted the provisions of Statement of Financial Accounting Standards (SFAS) No. 142, Goodwill and Other Intangible Assets effective January 1, 2002. Under SFAS No. 142, goodwill is reviewed at least annually for impairment. SFAS No. 142 requires that goodwill be tested for impairment at the reporting unit level at adoption and at least annually thereafter, utilizing a fair value methodology versus an undiscounted cash flow method required under previous accounting rules. In accordance with our adoption of SFAS No. 142, we completed an interim test at September 30, 2005 utilizing cash-flow based market comparables in assessing fair value for our goodwill impairment testing and we concluded that there was an impairment of our goodwill. To the extent that future cash flows differ from those projected in our analysis, fair value of our goodwill may be affected and may result in an impairment change.

Capitalized Software Development and Research and Development Costs incurred internally and fees paid to outside contractors and consultants during the application development stage of our internally used software products are capitalized. Costs of upgrades and major enhancements that result in additional functionality are also capitalized. Costs incurred for maintenance and minor upgrades are expensed as incurred. All other costs are expensed as incurred as research and development expenses and are included in selling, general and administrative expenses. Application development stage costs generally include software configuration, coding, installation to hardware and testing. Once the project is completed, capitalized costs are amortized over their remaining estimated economic life. Our judgment is used in determining whether costs meet the criteria for immediate expense or capitalization. We periodically review projected cash flows and other criteria in assessing the impairment of any internal-use capitalized software and take impairment charges as needed.

Purchased Technology and Other Intangibles Assets Purchased technology and other intangible assets are amortized on a straight line basis over their estimated useful lives of 4.6 to 12 years. The carrying values of purchased technology and intangible assets are reviewed if the facts and circumstances indicate that they may be impaired. This review indicates whether assets will be recoverable based on future expected cash flows, and, if not recoverable, whether there is an impairment of such assets.

Reserve for Doubtful Accounts/Revenue Allowances/Bad Debt Estimates We rely on estimates to determine revenue allowances, the bad debt expense and the adequacy of the reserve for doubtful accounts receivable. These estimates are based on our historical experience and the industry in which we operate. If the financial condition of our customers were to deteriorate, resulting in an impairment of their ability to make payments, additional allowances may be required. Additionally, in our Medical Cost Containment business, we evaluate the collectibility of our accounts receivable based on a combination of factors. In circumstances where we are aware of a specific customer s inability to meet its financial obligations to us, we record a specific reserve for bad debts against amounts due to reduce the net recognized receivable to the amount we reasonably believe will be collected. For all other customers, we recognize revenue reserves based on past write-off history, average percentage of receivables written off historically, and the length of time the receivables are past due. To the extent historical credit experience is not indicative of future performance or other assumptions used by management do not prevail, loss experience could differ significantly, resulting in either higher or lower future provision for losses.

New Accounting Pronouncements

In May 2005, the Financial Accounting Standards Board (FASB) issued SFAS No. 154, Accounting Changes and Error Corrections. SFAS No. 154 requires retrospective application of a voluntary change in accounting principle to prior period financial statements unless it is impractical. SFAS No. 154 also requires that a change in method of depreciation, amortization, or depletion for long-lived, non-financial assets be accounted for as a change in accounting estimate affected by a change in accounting principal. SFAS No. 154 replaces APB Opinion No. 20, Accounting Changes, and SFAS No. 3, Reporting Accounting Changes in Interim Financial Statements. SFAS No. 154 is effective for fiscal years beginning after December 15, 2005. We do not expect the adoption of the provision of SFAS No. 154 to have a material impact on our results of operations or financial condition.

In March 2005, the SEC issued SAB No. 107. This SAB provides guidance related to the application of SFAS No. 123R, Shared-Based Payments (Revised 2004) for transactions with non-employees, the transition from

32

Table of Contents

nonpublic to public entity status, valuation methods, the accounting for certain redeemable financial instruments issued under share-based payment arrangements, the classification of compensation expense, non-GAAP financial measures, first-time adoption of SFAS 123R and Disclosures in Management s Discussion and Analysis (MD&A) subsequent to adoption of SFAS 123R. The revised effective date of SFAS No. 123R is for annual reporting periods beginning after June 15, 2005. The adoption date for us is January 1, 2006. We have not completed the process of evaluating the impact that will result from adopting SFAS 123R and are therefore unable to disclose the impact that adoption will have on our financial position and results of operations.

In September 2004, the FASB issued EITF No. 04-8, Accounting Issues Related to Certain Features of Contingently Convertible Debt and the Effect on Diluted Earnings per Share (EITF No. 04-8). EITF No. 04-8 addresses when the dilutive effect of contingently convertible debt instruments should be included in diluted earnings per share and requires that contingently convertible debt instruments are to be included in the computation of diluted earnings per share regardless of whether the market price or other trigger has been met. EITF No. 04-8 also requires that prior period diluted earnings per share amounts presented for comparative purposes be restated. EITF No. 04-8 is effective for reporting periods ending after December 15, 2004. As a result of the issuance of EITF No. 04-8, shares convertible from our $13.1 million convertible notes may be required to be included in the calculation of our earnings per share in periods of net income; however, the FASB has yet to reach a conclusion as to the effect of non market price triggers on earnings per share calculations in situations where the instrument contains only non-market price triggers, such as our convertible notes, and therefore the impact on the consolidated financial statements is not determinable at this time.

In November 2004, the FASB issued SFAS No. 151, Inventory Costs, an amendment of ARB No. 43, Chapter 4. This Statement clarifies the accounting for abnormal amounts of idle facility expense, freight, handling costs, and spoilage and requires that those items be recognized as current-period charges regardless of whether they meet the criterion of so abnormal under ARB No. 43. The provisions of this Statement shall be effective for inventory costs incurred during fiscal years beginning after June 15, 2005. We do not expect the adoption of the provision of SFAS No. 151 to have a material impact on our results of operations or financial condition.

Cautionary Statement Pursuant to Safe Harbor Provisions of the Private Securities Litigation Reform Act of 1995

Statements contained in Management s Discussion and Analysis of Financial Condition and Results of Operations and elsewhere in this prospectus may contain information that includes or is based upon forward-looking statements within the meaning of the Securities Litigation Reform Act of 1995. Forward-looking statements present our expectations or forecasts of future events. These statements can be identified by the fact that they do not relate strictly to historical or current facts. They frequently are accompanied by words such as anticipate, estimate, expect, project, intend, plan, believe, and other words and terms of similar meaning. In particular, these include statements relating to: our ability to identify suitable acquisition candidates; our successful integration of MedUnite, PlanVista and any other future acquisitions; our ability to successfully develop, market, sell, cross-sell, install and upgrade our clinical and financial transaction services and applications to new and current physicians, payers, medical laboratories and pharmacies; our ability to compete effectively on price and support services; our ability to increase revenues and revenue opportunities; and our ability to meet expectations regarding future capital needs and the availability of credit and other financing sources.

All statements other than statements of historical fact are statements that could be deemed forward-looking statements, including any projections of earnings, revenues, synergies, accretion, margins or other financial items; any statements of the plans, strategies and objectives of management for future operations, including the execution of integration and restructuring plans and the anticipated timing of filings, approvals and closings relating to the merger or other planned acquisitions; any statements concerning proposed new products, services, developments or industry rankings; any statements regarding future economic conditions or performance; any statements of belief; and any statements of assumptions underlying any of the foregoing.

Actual results may differ significantly from projected results due to a number of factors, including, but not limited to, the soundness of our business strategies relative to perceived market opportunities; our assessment of the healthcare industry s need, desire and ability to become technology efficient; market acceptance of our products and

services; and our ability and that of our business associates to comply with various government rules regarding

Table of Contents

healthcare information and patient privacy. These and other risk factors are more fully discussed starting on page 6 and elsewhere in this prospectus, which we strongly urge you to read.

Forward-looking statements are not guarantees of performance. They involve risks, uncertainties and assumptions. Our future results and shareholder values may differ materially from those expressed in the forward-looking statements. Many of the factors that will determine these results and values are beyond our ability to control or predict. Shareholders are cautioned not to put undue reliance on any forward-looking statements. For those statements, we claim the protection of the safe harbor for forward-looking statements contained in the Private Securities Litigation Reform Act of 1995. We expressly disclaim any intent or obligation to update any forward-looking statements.

Table of Contents

QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Foreign Currency Risk

We own no derivative financial instruments or derivative commodity instruments. Revenue derived from international sales is transacted in U.S. Dollars, and therefore, we do not believe that we are exposed to material risks related to foreign currency exchange rates.

Interest Rate Risk

In the normal course of business, we are exposed to fluctuations in interest rates. We are establishing policies and procedures to manage this exposure through a variety of financial instruments. We will not enter into any contracts for the purpose of trading or speculation to manage this risk.

Credit Risk

We have a concentration of credit risk in each of our two operating segments which is further disclosed in Note 16 to the consolidated financial statements.

FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

The consolidated financial statements and schedule are included beginning at Page F-1.

CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

Effective August 11, 2004, PricewaterhouseCoopers LLP resigned as our independent registered certified public accounting firm. On August 11, 2004, our Audit Committee, in accordance with the Audit Committee Charter, announced that Deloitte and Touche LLP would be our independent registered public accounting firm effective immediately. We had not consulted with Deloitte & Touche LLP in the last two fiscal years or in any interim period through the date of the engagement with respect to any matters contained in Item 304(a)(2)(i) and (ii) of Regulation S-K.

The reports of PricewaterhouseCoopers LLP on our financial statements as of and for the fiscal years ended December 31, 2003 and 2002 contained no adverse opinion or disclaimer of opinion, and were not modified as to uncertainty, audit scope or accounting principle.

During the two fiscal years ended December 31, 2003 and 2002 and through August 11, 2004, there were no disagreements with PricewaterhouseCoopers LLP on any matter of accounting principles or practices, financial statement disclosure, or auditing scope or procedure, which disagreements, if not resolved to the satisfaction of PricewaterhouseCoopers LLP, would have caused PricewaterhouseCoopers LLP to make reference thereto in their report on the financial statements for such years.

During the two fiscal years ended December 31, 2003 and 2002 and through August 11, 2004, there were no reportable events (as defined in Item 304(a)(1)(v) of Regulation S-K under the Securities Exchange Act of 1934).

In response to our request, PricewaterhouseCoopers LLP furnished us with a letter addressed to the Securities and Exchange Commission stating whether or not it agrees with the above statements. A copy of such letter dated August 16, 2004, was attached as Exhibit 16.1 to our Form 8-K filed on August 17, 2004.

Table of Contents

CONTROLS AND PROCEDURES

Disclosure Controls and Procedures:

Our management, under the supervision and with the participation of the our Chief Executive Officer (CEO) and Chief Financial Officer (CFO), have evaluated the effectiveness of our disclosure controls and procedures as defined in Securities and Exchange Commission (SEC) Rule 13a-15(e) as of the end of the period covered by this report. Management has concluded that our disclosure controls and procedures are effective to ensure that information that we are required to disclose in reports that we file or submit under the Securities Exchange Act is communicated to management, including the CEO and CFO, as appropriate, to allow timely decisions regarding required disclosure and is recorded, processed, summarized, and reported within the time periods specified in the SEC s rules and forms.

Changes in Internal Control

There have been no changes to our internal control over financial reporting that occurred during the fourth quarter of 2004, or subsequently, that have materially affected, or are reasonably likely to materially affect our internal control over financial reporting.

Management s Annual Report On Internal Control Over Financial Reporting:

Our management is responsible for establishing and maintaining adequate internal control over financial reporting for us. Our internal control over financial reporting is a process designed by, or under the supervision of, our CEO and CFO, and affected by our Board of Directors, management, and other personnel to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. Our internal control over financial reporting includes those policies and procedures that:

(1) pertain to the maintenance of records that in reasonable detail accurately and fairly reflect our transactions and dispositions of our assets;

(2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of consolidated financial statements in accordance with generally accepted accounting principles, and that our receipts and expenditures are being made only in accordance with authorizations of our management and board of directors; and

(3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of our assets that could have a material effect on the consolidated financial statements.

Internal control over financial reporting cannot provide absolute assurance of achieving financial reporting objectives because of its inherent limitations. Internal control over financial reporting is a process that involves human diligence and compliance and is subject to lapses in judgment and breakdowns resulting from human failures. Internal control over financial reporting also can be circumvented by collusion or improper management override. Because of such limitations, there is a risk that material misstatements may not be prevented or detected on a timely basis by internal control over financial reporting. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate. However, these inherent limitations are known features of the financial reporting process. Therefore, it is possible to design into the process safeguards to reduce, though not eliminate, this risk.

Management uses the framework in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission, or COSO, to evaluate the effectiveness of our internal control over financial reporting. Management assessed our internal control over financial reporting using the COSO framework as of the end of our fiscal year. Based on our evaluation under the framework in Internal Control Integrated Framework, we believe our internal control over financial reporting as of December 31, 2004 was effective. Management s assessment of the effectiveness of internal control over financial reporting as of

Table of Contents

December 31, 2004 has been audited by Deloitte & Touche LLP, an independent public registered accounting firm, which also audited our 2004 consolidated financial statements. Deloitte & Touche LLP s attestation report on management s assessment of internal control over financial reporting is set forth herein.

Table of Contents

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Stockholders of
ProxyMed, Inc.
Atlanta, Georgia

We have audited management s assessment, included in the accompanying Management s Annual Report on Internal Control over Financial Reporting, that ProxyMed, Inc. and its subsidiaries (the Company) maintained effective internal control over financial reporting as of December 31, 2004, based on criteria established in Internal Control Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission. The Company s management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting. Our responsibility is to express an opinion on management s assessment and an opinion on the effectiveness of the Company s internal control over financial reporting based on our audit.

We conducted our audit 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 effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, evaluating management s assessment, testing and evaluating the design and operating effectiveness of internal control, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinions.

A company s internal control over financial reporting is a process designed by, or under the supervision of, the company s principal executive and principal financial officers, or persons performing similar functions, and effected by the company s board of directors, management, and other personnel to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company s internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company s assets that could have a material effect on the financial statements.

Because of the inherent limitations of internal control over financial reporting, including the possibility of collusion or improper management override of controls, material misstatements due to error or fraud may not be prevented or detected on a timely basis. Also, projections of any evaluation of the effectiveness of the internal control over financial reporting to future periods are subject to the risk that the controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, management s assessment that the Company maintained effective internal control over financial reporting as of December 31, 2004, is fairly stated, in all material respects, based on the criteria established in Internal Control Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission. Also in our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2004, based on the criteria established in Internal Control Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated financial statements and financial statement schedule as of and for the year ended December 31, 2004 of the Company, and our report dated March 16, 2005 expressed an unqualified opinion on those consolidated financial statements and financial statement schedule and included an explanatory paragraph concerning matters that raise substantial doubt about the Company s ability to continue as a going concern.

/s/ Deloitte & Touche LLP
Atlanta, GA
March 16, 2005

38

Table of Contents

BUSINESS

We were incorporated in Florida in 1989. In December 2005, we announced that we would be doing business under a new operating name, MedAvant Healthcare Solutions (MedAvant). Our newly launched corporate identity unites all business units and employees under one brand identity, MedAvant, and is one of several outcomes resulting from a strategic analysis we completed in the third quarter of 2005 following the acquisition of seven companies between 1997 and 2004.

MedAvant is a healthcare transaction processing company, providing comprehensive suites of products and services for providers, payers, pharmacies, medical laboratories, and other healthcare suppliers. Our solutions take a holistic approach to our customers needs. We seek to resolve their business challenges by looking at their entire business process, not just parts of it, leveraging each area to help them realize a positive result to their bottom line. Our business strategy is to use our market leadership position in healthcare transactions service; cost containment; payer, provider and clinical connectivity; and business process outsourcing to develop and promote holistic products and services that actually escalate our customers success. We seek to not just meet their needs, but to help them realize a higher level of success by encompassing their business as a whole. Indeed we are the only healthcare technology company that offers both a nationwide claims clearinghouse and a nationwide PPO network.

We are uniquely positioned in our marketplace to make a contribution that our competitors do not. Our differentiators include our proprietary technology, including *Phoenix*SM and *Pilot*SM, and out ability to offer a nationwide claims clearinghouse and a nationwide PPO network. In addition, we maintain an open, neutral position with vendors, which allows us to attract partners who prefer a non-competitive environment. This also allows us to offer more flexible options for our customers. Another differentiator is our deep footprint in the clinical arena. With the nation s largest clinical laboratories as long-time customers, we have worked in partnership with them to develop customized lab communication tools and services. Also, our prescription business operates the nation s largest and longest-established electronic and fax gateway infrastructure with extensive connectivity to all major pharmacies in the nation.

We provide two reportable segments that are separately managed: Transaction Services and Laboratory Communication Solutions. Transaction Services includes transaction, cost containment, business process outsourcing and other value-added services principally between physicians and insurance companies, and physicians and pharmacies. Laboratory Communication Solutions includes the sale, lease and service of communication devices principally to laboratories and through June 30, 2004, the contract manufacturing of printed circuit boards. Commencing in March 2004, the operations of PlanVista are included in our Transaction Services segment.

A more complete description of the products and services of each of our segments begins on page 42 below. For information regarding the results of operations of each of our segments, see Management s Discussion and Analysis of Financial Condition and Results of Operations beginning on page 17.

Our electronic transaction processing services support a broad range of financial, clinical, and administrative transactions. To facilitate these services, we are completing the conversion of all of our non-clinical electronic healthcare transaction clients to *Phoenix*SM, our secure, real-time proprietary national electronic information network, which provides physicians and other healthcare providers with direct connectivity to one of the industry s largest lists of payers.

Our cost containment and business process outsourcing solutions, included in the Transaction Services segment, is directed toward the medical insurance and managed care industries. Specifically, we provide integrated national PPO network access, electronic claims repricing, and network and data management to healthcare payers, including self insured employers, medical insurance carriers, PPOs and Third Party Administrators.

Our corporate headquarters is located in Norcross, Georgia, and our products and services are provided from various operational facilities located throughout the United States. We also operate our clinical computer network and portions of our financial and real-time production computer networks from a secure, third-party co-location site located in Atlanta, Georgia.

Table of Contents

Our Changing Market

Payers using electronic healthcare transactions fit into two traditional categories: participating and non-participating. Participating payers, including commercial (private) payers as well as a number of Blue Cross and Blue Shield plans traditionally pay companies like us a fee for delivering electronic transactions to them. This allows us to offer the transactions free to submitting providers. We believe that this allows payers to save anywhere from 50 cents to more than $2 over the cost of handling a paper transaction, and up to $5 over the cost of a phone call. This market approach is a win-win for providers and payers to date, as payer subsidies encourage providers to submit transactions electronically. Providers submitting electronically can benefit from fewer processing delays for payment.

In contrast, non-participating payers, traditionally government payers such as Medicare and Medicaid and some Blue Cross and Blue Shield plans, do not pay transaction fees. In most cases, providers pay the cost of transmitting their non-participating claims or other transactions to these payers when processed through a clearinghouse.

Our provider solutions are focused on self-service tools, and improved service levels. We have invested millions of dollars in our processing platform called *Phoenix*SM, which will support modern self-service and drill down tool capability. Our suite of new Web-based self-service tools provides revenue management and claims tracking. These new tools allow providers to access details of individual claims to confirm receipt by the payer and any error information for rejected claims.

Over the course of 2005, we made substantial progress on the integration of all products and services into one suite of services residing on one platform, *Phoenix*SM. This integration enhanced our ability to support multiple technologies that our providers and payers use. This suite of products covers platforms as old as DOS but also includes solutions for those that have the latest in Internet platforms.

Industry Growth

According to the Centers for Medicare and Medicaid Services, referred to as CMS, health spending growth actually slowed in 2003, the first deceleration in seven years. United States healthcare expenditures grew 7.7% in 2003 to $1.7 trillion, which is down from 9.3% growth in 2002. CMS projects that national health expenditures will reach $3.4 trillion by 2013.

Per capita, health spending increased in 2003 by $353 to $5,670

Health spending accounted for 15.3% of GDP in 2003

Health spending outpaced growth in the overall economy by 3 percentage points

According to *Modern Healthcare s* By the Numbers (December 20, 2004), 22% of the nation s healthcare dollars went to physician and clinical services, with 7% going to administrative costs. As one of the most transaction-oriented industries in the country, analysts report that healthcare generates over 35 billion financial and clinical transactions each year, including new prescription orders, refill authorizations, laboratory orders and results, medical insurance claims, insurance eligibility inquiries, encounter notifications, and referral requests and authorizations. Current healthcare information technology spending has been projected at $41.6 billion for 2004, and is predicted to continue growing steadily at 7% annually through 2006. Even with healthcare information technology spending at these levels, we believe that the healthcare industry s use of technology lags behind many other transaction-intensive industries, with the vast majority of these healthcare transactions being performed manually and on paper.

For physician offices, payers, laboratories and pharmacies to meet the financial, clinical and administrative demands of an evolving managed care system, we believe that they will need to process many of these types of transactions electronically. The Health Insurance Portability and Accountability Act of 1996, referred to as HIPAA (see Healthcare and Privacy Related Legislation and regulation below) establishes electronic standards for eight

Table of Contents

major transaction types, including claims, eligibility inquiries and claims status inquiries. Our secure, proprietary systems provide an electronic link between healthcare payers and healthcare providers such as laboratories, hospitals, and physician office practices for these transactions.

Key Competitive Strengths

We believe we have competitive advantages in four critical areas:

(1) Our solutions are encompassing. We seek to resolve our customers business challenges by looking at their entire business process, leveraging each area to help them realize a positive result to their bottom line. We are the only healthcare technology company that offers both a nationwide claims clearinghouse and a nationwide PPO network. We use our market leadership position in cost containment services, payer, provider and clinical connectivity, and business process outsourcing, to develop and promote comprehensive products and services that actually escalate our customers success.

(2) Our technology is superior. Phoenix[SM], our transaction processing platform, is a highly scalable secure national information platform, which supports real-time and batch transaction processing between our healthcare clients. Built internally three years ago from the ground-up, Phoenix s robust throughput and scalability make it unique, but the value truly lies in the time and cost it saves our clients. Phoenix is HIPAA-compliant and supports a broad range of financial and clinical transactions. In addition, Pilot is a smart routing delivery device that was built internally last year on a Linux operating system. Pilot is a physical device that allows our lab clients to send lab reports to providers in virtually any format, from PDF to PCL, TIFF, JPG, and Zip, opening the door to product differentiating factors such as graphical and color reporting.

(3) Our connectivity is extensive. Our broad existing connectivity to payers and providers positions us as the second largest independent medical claims clearinghouse in the industry. We have almost 150,000 providers using our claims processing solutions, and an additional 450,000 contracted directly and indirectly for our PPO Network, NPPN[SM]. To reach these direct and partnered providers, we have licensing and connectivity agreements with many national and regional companies, such as practice management system vendors, billing services, and electronic healthcare companies, and with physician offices directly. These relationships offer us an opportunity to cross-sell our products and services to our existing provider customer base. Our electronic healthcare transaction services support a broad range of financial transactions (such as claims, patient statements, claims status reports, eligibility verification, explanations of benefits and electronic remittance advices); clinical transactions (such as laboratory results, new prescription orders and prescription refills); and administrative transactions (such as referrals and pre-certifications). These connections allow information to reliably move back and forth from the provider office to the appropriate healthcare institution (payer, laboratory and pharmacy) facilitating diagnosis, treatment and payment. We are also the largest provider of intelligent laboratory results reporting devices and the nation s largest provider of retail pharmacy clinical connectivity.

(4) Our PPO network is national in scope. We believe that our PPO network, which is comprised of both directly contracted providers and those accessed through our regional network partners, is the second largest in the nation in terms of number of providers (physicians, hospitals and ancillary providers) contracted. In terms of managed care lives accessing our network, we are currently ranked sixth in the nation.

Barriers to Entry

We have expended considerable time, effort and expense developing the infrastructure, relationships, and interoperability of our back-end connectivity for both financial and clinical transactions. We believe that the cost and time demands of development and maintenance of the connections from both a technical and relationship perspective represent a barrier to entry for would-be competitors.

Table of Contents

Current Products and Services

In our Transaction Services segment, we offer products and services for payers (both government and commercial insurance companies), providers (physicians and hospitals) and clinical institutions (pharmacies, clinical laboratories, others). We also provide medical cost containment and business process outsourcing solutions for the medical insurance and managed care industries. These new products are the foundation for our suite of solutions to our payer customers. These customers include healthcare payers such as self-insured employers, medical insurance carriers, third party administrators, Health Maintenance Organizations, referred to as HMOs, and other entities that pay claims on behalf of health plans. Our payer-focused solutions also include network and data management business process outsourcing services for providers, including individual providers, PPOs , and other provider groups.

Our provider-focused suite of solutions include electronic healthcare transaction services designed to interconnect with diverse technologies and connection capabilities. This suite of products covers platforms as old as DOS but also includes solutions for those that have the latest in Internet platforms. Our solutions are available through our suite of Windows-based products (1), through our Internet portal, *Envision* , and through various direct network connection programs. Each of these entry points connects providers to our network and then routes transactions to their contracted payer, laboratory and pharmacy partners.

Our provider solutions include claims submission and reporting, insurance eligibility verification, claims status inquiries, referral management, laboratory test results reporting and prescription refills, all available today through *Medavanthealth.net*. We continue to expand our offerings through our portal to include new financial and clinical transactions such as claims response management, electronic remittance advices, encounters and new prescriptions. All of our existing Web-based applications can be private-labeled and are being marketed through our channel partners to increase distribution opportunities.

(1) Windows is a registered trademark of Microsoft Corporation.

Transaction Services

Payer Services

Through our acquisition of PlanVista, we provide medical cost containment and business process outsourcing solutions for the medical insurance and managed care industries. These new products are part of the foundation for our suite of solutions to our payer customers. These customers include healthcare payers such as self-insured employers, medical insurance carriers, third party administrators, HMOs, and other entities that pay claims on behalf of health plans. We also provide network and data management business process outsourcing services for healthcare providers, including individual providers, PPOs, and other provider groups.

ClaimPassXL® is our Internet claims repricing system and allows us to shift claims repricing submissions from paper or fax to the Internet, which reduces claims processing costs significantly. Faster turnaround of claims repricing will become more important to payers as state insurance regulators increase their scrutiny of claims payment turnaround times.

National Preferred Provider Network The National Preferred Provider Network, referred to as NPPN, is a nationwide physician network comprised of PPOs, independent physician associations, and individually contracted providers that agree to offer discounts on medical services. These providers and provider groups participate in NPPN to increase patient flow and benefit from NPPN s prompt, efficient claims repricing services. Healthcare payers access NPPN to benefit from the discounts offered by participating providers. The size of NPPN and the level of NPPN discounts provide our payer customers with significant reductions in medical claims costs.

NPPN access agreements generally require our customers to pay us a percentage of the cost savings generated by NPPN discounts. In the medical cost containment industry, this payment arrangement is called a percentage of savings revenue model. A typical percentage of savings customer maintains arrangements with more than one PPO network. Most of these payer customers utilize NPPN as an additional network to contain costs when a covered person obtains medical services from a provider outside of the payer s primary PPO network. When

Table of Contents

we receive a provider bill for medical services that are covered by NPPN discount arrangements, we electronically reprice it to conform to the negotiated discounted rate, which is typically lower than the invoiced amount. We derive the balance of our NPPN operating revenue from payer customers that pay a flat fee per month based on the number of enrolled members. These customers generally access the NPPN as their primary PPO network. More than 80% of our participating providers have been part of NPPN for more than three years, with some relationships spanning more than nine years since the beginning of NPPN s inception in 1994.

Electronic Claims Repricing In connection with our NPPN access business, we provide electronic claims repricing services that benefit both our payer clients and our participating providers. A participating provider submits a claim at the full, undiscounted provider rate. The provider sends the claim directly to us or to the payer which then forwards the bill to us. Because there is a wide variety of provider systems for submitting claims, we accept claims by traditional methods such as mail and fax, as well as through the Internet and by our electronic transaction services. We convert paper and faxed claims to an electronic format, and then electronically reprice the claims by calculating the reduced price based on our NPPN s negotiated discount. We return the repriced claims file to the payer electronically, in most cases within three business days.

Network and Data Management We use our information system capabilities to provide network and data management services for the payers that access NPPN. For some network access payers, we act as the payer s mailroom for receipt of all provider claims, converting paper and fax claims to an electronic format, identifying the correct network fee schedule applicable to each claim, and electronically repricing the claim accordingly. We prepare detailed reports regarding repricing turnaround times and the savings that each payer realizes, itemized by the total number of claims incurred, number of claims discounted, and the average discount. Payers can use this information to help design health plans that effectively control costs, enhance member benefits, and yield a more favorable loss ratio (ratio of paid medical claims compared to collected premiums). We integrate several components of certain licensed reporting software to provide both payer clients and participating PPOs with quick access to claims data, allowing them to produce a variety of analytical reports. We generally do not charge our NPPN access customers any additional fee for our standard network and data management services.

Bill Review and Negotiation We offer optional medical bill review and negotiation services to our payer clients. Many of our percentage of savings clients send us all claims that fall outside their primary PPO network arrangements. We offer payer customers the opportunity to realize cost savings on these out-of-network claims through our affiliations with bill review and negotiation companies. We can electronically transmit non-NPPN claims to experienced professionals at the contracted bill review and negotiation companies. These professionals use proprietary medical software to analyze each claim to detect any incorrect charges or billing irregularities. Once that phase of the analysis is completed, the detailed charges are compared to a proprietary database to determine the competitiveness of the charges in the provider s geographic area. The bill negotiator then contacts the provider to discuss the findings, and in many cases is able to reduce the claim amount. The reviewer obtains signed agreements from each provider to prevent the provider from later contesting the reduction or billing the patient for the balance. The bill review and negotiation vendor then returns the electronic file to us, and we forward it to the payer along with the payer s other repriced claims. Payers pay us a percentage of the savings that are generated by the bill review and negotiation service.

Business Process Outsourcing We traditionally provided claims repricing and network management services only with respect to claims that NPPN participating providers submitted to one of our network access payer customers. Through our network and data management outsourcing business, we have expanded our scope to offer payers and providers services that are independent of our network access business.

Desktop We offer several Windows and Unix based desktop products, including claims submission and tracking. Unix is a registered trademark of The Open Group.

Online For providers who prefer to use Internet based services, we developed and have been operating our provider transaction services Web portal, *Medavanthealth.net,* for over five years. *Medavanthealth.net s* available Web-based financial and administrative transactions now include:

claims submission and reporting;

Table of Contents

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eligibility verification;

claims status inquiries;

ERA;

referral management; and

pre-certifications.

Real-Time Our real-time suite of solutions provides a quick and easy way to streamline the patient registration process, insuring more accurate payment information through pre-certification, and to check the status of claims. Our real-time suite includes:

eligibility verification and benefits inquiry;

referral authorization and pre-certifications;

claim status inquiry.

B2B In addition to working directly with providers, we offer software developers, large customers and partners an Application Programming Interface (API) to connect to our real-time transaction platform and directly submit XML or X12 based transactions. This service is sold as our business-to-business (B2B) offering. The platform which supported the B2B offering was based on a proprietary XML transaction format and is HIPAA compliant.

Prescription Services

We offer both new prescription ordering and refill management through our *PreScribe*® family of products. There are currently over 4,000 physician clients using *PreScribe*. *PreScribe* and *Phoenix*SM support the largest and oldest electronic and fax gateway infrastructure with connectivity to over 37,000 pharmacies nationwide. We also offer a private-label version of our Web-based refill prescription application.

Laboratory Communication Solutions

Our Laboratory Communication Solutions segment is an integral part of our connectivity to the healthcare industry. We engineer, and provide communication devices for clinical laboratories throughout the United States. We have over 100,000 devices in use in provider offices nationwide, providing unmatched service and reliability in the way they deliver patient lab reports. This direct connectivity into the physician office provides a critical link in the patient diagnosis and treatment cycle.

Product and Services Development

Our goal is to drive all of our customers to our portal where they can access all of our products and services. For both of our segments, Transaction Services and Laboratory Communication Solutions, we are currently augmenting Medavanthealth.net, our new online portal. These additions include customer-based products and services, along with multi-functional self-service tools.

We are uniquely positioned in the clinical laboratory industry with the onset of our new *Pilot*SM and *Navigator*SM solutions. *Pilot* was released in the first quarter of 2005 and provides enhanced reporting processes for results delivery to clinical laboratories. This product allows labs to customize report delivery, and to export results to their Electronic Medical Record and Practice Office Management Information System. They can review their results via Internet or dial-up. We have deployed over 4,500 of these devices since Pilot s release. Pilot s companion product, *Navigator*, provides the supportability function of fleet monitoring, usability data, and uptime management for remote printer devices. *Navigator* was released in the second quarter of 2005.

Table of Contents

The total amount capitalized for purchased technology, capitalized software and other intangible assets as of September 30, 2005 and December 31, 2004, was approximately $18.7 million and $52.3 million, respectively, net of amortization.

Marketing

We have a direct sales force and customer support staff that serves payers, providers, clinical laboratories and pharmacies. In addition, since we do not compete for the physician desktop and allow for private branding of our value-added products and services, we are able to leverage the marketing and sales efforts of our partners by giving them even greater added value to drive our revenues and transactions.

We utilize the following distribution channels for our products and services to maximize connectivity between physician offices, payers, laboratories, pharmacies and other healthcare providers:

Channel Focus	
Direct	We have a direct sales force of account executives, inside telemarketers, account managers and customer care representatives who serve our providers, payers, laboratories and pharmacies. We license access to our proprietary network, Phoenix , and provide intelligent laboratory results reporting devices for communications between providers and clinical laboratories.
Partners	We work with the vendors of POMIS and pharmacy office management systems so that they may enable their existing applications to process transactions through us between providers and payers, laboratories and pharmacies. We also license these customers to offer our products and services under their own private label. In addition, we connect with other electronic transaction processing networks so that the participants on both networks can communicate with each other in National Council of Pharmacy Drug Program standard, HIPAA approved formats, and the HL-7 standard format for laboratories.
Internet	We provide comprehensive suites of products for financial, clinical and administrative transaction processing services through our portal, MedAvanthealth.net, which may be easily accessed by any payer, provider or business partner with an Internet connection. We are currently in development to customize those products by customer, so that every solution a payer will want to use will be available on one easy-to-use site. There will also be a customized portal for providers and partners.

Competition

Transaction Services We face competition from many healthcare information systems companies and other technology companies. Many of our competitors are significantly larger and have greater financial resources than we do and have established reputations for success in implementing healthcare electronic transaction processing systems. Other companies, including EMDEON, NDCHealth Corporation, Per-Se Technologies, and other healthcare related entities have targeted this industry for growth, including the development of new technologies utilizing Internet-based systems. While our ability to compete has been enhanced by our unique national offerings and proprietary offerings, we cannot assure that we will be able to compete successfully with these companies or that these or other competitors will not commercialize products, services or technologies that render our products, services or technologies obsolete or less marketable.

Preferred Provider Network The PPO industry is highly fragmented. According to the American Association of Preferred Provider Organizations, as of March 2003 there were more than 1,000 PPOs in the United States. A few companies, such as First Health Group Corporation, Preferred Medical Claims/eHealth Solutions, Concentra, Inc., Coalition America, Inc., and Multiplan, Inc., offer provider networks and claim volumes of meaningful size. The remainder of the competitive landscape is diverse, with major insurance companies and managed care organizations such as Blue Cross and Blue Shield plans, Aetna, WellPoint Health Networks, Inc., UnitedHealth Group, Humana Health Care Plans, private healthcare systems, and CIGNA Healthcare also offering proprietary preferred provider networks and services. In addition, the number of independent PPOs has decreased as managed care organizations and

large hospital chains have acquired PPOs to administer their managed care business

Table of Contents

and increase enrollment. We expect consolidation to continue as the participants in the industry seek to acquire additional volume and access to PPO contracts in key geographic markets. This consolidation may give customers greater bargaining power and lead to more intense price competition.

Electronic Claims Repricing The claims repricing service market is also fragmented. Our repricing competitors provide some or all of the services that we currently provide. Our competitors can be categorized as follows:

large managed care organizations and third party administrators with in-house claims processing and repricing systems, such as Blue Cross and Blue Shield plans, UnitedHealth Group, and Wellpoint Health Networks; and

healthcare information technology companies providing enterprise-wide systems to the payer market, such as MultiPlan, McKesson Corporation and Perot Systems Corporation.

The market for claims repricing services is competitive, rapidly evolving, and subject to rapid technological change. We believe that competitive conditions in the healthcare information industry in general will lead to continued consolidation as larger, more diversified organizations are able to reduce costs and offer an integrated package of services to payers and providers.

We compete on the basis of the strength of our electronic claims repricing technology, the size of our network and the level of our network discounts, our percentage of savings pricing model, and the diversity of services we offer through our business processing outsourcing products and other new initiatives. Many of our current and potential competitors have greater financial and marketing resources than we have. Furthermore, we believe that the increasing acceptance of managed care in the marketplace, the adoption of more sophisticated technology, legislative reform, and the consolidation of the industry will result in increased competition. There can be no assurance that we will continue to maintain our existing customer base, or that we will be successful with any new products that we have introduced or will introduce.

Healthcare and Privacy Related Legislation and Regulation

We and our customers are subject to extensive and frequently changing federal and state healthcare laws and regulations. Political, economic and regulatory influences are subjecting the healthcare industry in the United States to fundamental change. Potential reform legislation may include:

mandated basic healthcare benefits;

controls on healthcare spending through limitations on the growth of private health insurance premiums and Medicare and Medicaid reimbursement;

the creation of large insurance purchasing groups;

fundamental changes to the healthcare delivery system;

enforcement actions of Federal and State privacy laws;

Medicare or Medicaid prescription benefit plans;

State licensing requirements; or

patient protection initiatives.

Table of Contents

HIPAA

Several state and federal laws govern the collection, dissemination, use and confidentiality of patient healthcare information. The federal Health Insurance Portability and Accountability Act of 1996, referred to as HIPAA, was signed into law on August 21, 1996. HIPAA was designed to improve the efficiency and effectiveness of the healthcare system by standardizing the interchange of electronic data for certain administrative and financial transactions and to protect the confidentiality of patient information. Multiple regulations have been and will continue to be, promulgated from this revolutionary legislation.

Privacy Compliance

HIPAA s Privacy Rule imposes extensive requirements on healthcare providers, healthcare clearinghouses, and health plans. These Covered Entities must implement standards to protect and guard against the misuse of individually identifiable health information. Certain functions of the Company have been or may be deemed to constitute a clearinghouse as defined by the Privacy Rule. However, in many instances, the Company also functions as a Business Associate of its health plan and provider customers. Among other things, the Privacy Rule requires us to adopt written privacy procedures, adopt sufficient and reasonable safeguards, and provide employee training with respect to compliance. Although we have undertaken several measures to ensure compliance with the privacy regulation and believe that we are in compliance, the privacy regulations are broad in scope, and will require constant vigilance for ongoing compliance.

We also may be subject to state privacy laws, which may be more stringent than HIPAA in some cases.

Transaction and Code Sets Compliance

HIPAA also mandates the use of standard transactions for electronic claims and certain other healthcare transactions. The U.S. Department of Health and Human Services published regulations to govern eight of the most common electronic transactions involving health information. As a clearinghouse, we must comply with these regulations. However, covered entities, including us and our physician and payer customers, are permitted to continue to process non-compliant transactions after October 16, 2003 so long as that covered entity is compliant with the contingency planning guidelines provided by the CMS.

Security Compliance

HIPAA s Security Rule imposes standards for the security of electronic protected health information. The effective date for the Security Rule was April 20, 2005. We have implemented physical, technical and administrative safeguards for the protection of electronic protected health information. The Security Rule also introduced the concept of an addressable implementation standard, which requires ongoing vigilance to ensure that employed safeguards are sufficient given current technology capabilities and threats and reasonable industry expectations. Current internal and external security auditing procedures have addressed both the required and the addressable implementation specifications by conducting risk assessments and implementing appropriate safeguards to mitigate any apparent gaps.

Identifiers

On January 24, 2004, rules on implementation of a national provider identification number were published. This rule mandates the use of a single identifier for all healthcare providers throughout the United States by 2007. Because our customers use a variety of identification numbers today, we anticipate some modification to our transaction handling formats and processes to handle a new single identifier. Alterations to our systems will require some development cost, and we could lose customers if we are not ready on time to handle the national provider identifier.

Gramm-Leach-Bliley

Table of Contents

Some of our customers may also be subject to the federal Gramm-Leach-Bliley Act, relating to certain disclosures of nonpublic personal health information and nonpublic personal financial information by insurers and health plans.

Internet Privacy and Regulation

Another area in which regulatory developments may impact the way we do business is privacy and other federal, state and local regulations regarding the use of the Internet. We offer a number of Internet-related products. Internet user privacy and the extent to which consumer protection and privacy laws apply to the Internet is an area of uncertainty in which future regulatory, judicial and legislative developments may have a significant impact on the way we do business, including our ability to collect, store, use and transmit personal information. Internet activity has come under heightened scrutiny in recent years, including several investigations in the healthcare industry by various state and federal agencies, including the Federal Trade Commission.

Patient/Consumer Protection Initiatives

State and federal legislators and regulators have proposed initiatives to protect consumers covered by managed care plans and other health coverage. These initiatives may result in the adoption of laws related to timely claims payment and review of claims determinations. These laws may impact the manner in which we perform services for our clients.

Provider Contracting and Claims Regulation

Some state legislatures have enacted statutes that govern the terms of provider network discount arrangements and/or restrict unauthorized disclosure of such arrangements. Legislatures in other states are considering adoption of similar laws. Although we believe that we operate in a manner consistent with applicable provider contracting laws, there can be no assurance that we will be in compliance with laws or regulations to be promulgated in the future, or with new interpretations of existing laws.

Many of our customers perform services that are governed by numerous other federal and state civil and criminal laws, and in recent years have been subject to heightened scrutiny of claims practices, including fraudulent billing and payment practices. Many states also have enacted regulations requiring prompt claims payment. To the extent that our customers reliance on any of the services we provide contributes to any alleged violation of these laws or regulations, then we could be subject to indemnification claims from its customers or be included as part of an investigation of its customers practices. Federal and state consumer laws and regulations may apply to us when we provide claims services and a violation of any of these laws could subject us to fines or penalties.

Licensing Regulation

We are subject to certain state licensing requirements for the services we provide through NPPN. Some states require our PPO business to formally register and file an annual or one-time accounting of networks and providers with which we contract. Given the rapid evolution of healthcare regulation, it is possible that we will be subject to future licensing requirements in any of the states where we currently perform services, or that one or more states may deem our activities to be analogous to those engaged in by other participants in the healthcare industry that are now subject to licensing and other requirements, such as third party administrator or insurance regulations. Moreover, laws governing participants in the healthcare industry are not uniform among states. As a result, we may have to undertake the expense and difficulty of obtaining any required licenses, and there is a risk that we would not be able to meet the licensing requirements imposed by a particular state. It also means that we may have to tailor our products on a state-by-state basis in order for our customers to be in compliance with applicable state and local laws and regulations.

Summary

We anticipate that Congress and state legislatures will continue to review and assess alternative healthcare delivery systems and payment methods, as well as Internet and healthcare privacy legislation, and that public debate of these issues will likely continue in the future. Because of uncertainties as to these reform initiatives and their

Table of Contents

enactment and implementation, we cannot predict which, if any, of such reform proposals will be adopted, when they may be adopted or what impact they may have on us.

While we believe our operations are in material compliance with applicable laws as currently interpreted, the regulatory environment in which we operate may change significantly in the future, which could restrict our existing operations, expansion, financial condition or opportunities for success.

Additional current HIPAA and privacy compliance information can be found on our website at www.medavanthealth.net.

Intellectual Property and Technology

In large part, our success is dependent on our proprietary information and technology. We rely on a combination of contracts, copyright, trademark and trade secret laws and other measures to protect our proprietary information and technology. We have rights under a number of patent applications filed by us or our acquired entities, in addition to rights under various trademarks and trademark applications. We acquired a number of copyright registrations covering our various software and proprietary products. As part of our confidentiality procedures, we generally enter into nondisclosure agreements with our employees, distributors and customers, and limit access to and distribution of our software, databases, documentation and other proprietary information. We cannot assure that the steps taken by us will be adequate to deter misappropriation of our proprietary rights or that third parties will not independently develop substantially similar products, services and technology. Although we believe our products, services and technology do not infringe on any proprietary rights of others, as the number of software products available in the market increases and the functions of those products further overlap, we and other software and Internet developers may become increasingly subject to infringement claims. These claims, with or without merit, could result in costly litigation or might require us to enter into royalty or licensing agreements, which may not be available on terms acceptable to us.

Employees

As of September 30, 2005, we employed 395 employees. We are not and never have been a party to a collective bargaining agreement. We consider our relationship with our employees to be good.

Legal Proceedings

In December of 2001, Insurdata Marketing Services, Inc., referred to as IMS, filed a lawsuit against HealthPlan Services, Inc., referred to as HPS, a former subsidiary of PlanVista, for unspecified damages in excess of $75,000. The complaint alleges that HPS failed to pay commissions to IMS pursuant to an arbitration award rendered in 1996. On January 10, 2005, the court granted summary judgment to IMS on the issue of liability for the arbitration award. We filed an appeal on the issue of liability. On September 26, 2005 we entered into a settlement to pay a total of $775,000 in exchange for a release from the entire claim, with an initial payment of $225,000 and the rest due in equal installments over five subsequent months. We are paying these installments in accordance with the settlement agreement.

In early 2000, four named plaintiffs filed a class action against Fidelity Group, Inc., referred to as Fidelity, HPS, Third Party Claims Management, and others, for unspecified damages, and the action is currently pending in the United States District Court for the District of South Carolina, Charleston division. The complaint stems from the failure of a Fidelity insurance plan, and alleges unfair and deceptive trade practices; negligent undertaking; fraud; negligent misrepresentation; breach of contract; civil conspiracy; and RICO violations against Fidelity and its contracted administrator, HPS. Two principals of the Fidelity plan have been convicted of insurance fraud and sentenced to prison in a separate proceeding. The class was certified and such certification was eventually upheld on appeal. Shortly after the case was remanded to the trial judge as a certified class for further discovery, we filed a motion to de-certify the matter based upon evidence not available to the trial judge when he first certified the class. While that motion was pending, the parties agreed to mediate the case before the trial judge. The mediation was successful and the parties agreed orally to settle the matter. We believe that our obligations under the settlement will be paid by our insurance carrier. Although we are currently working to finalize a formal settlement agreement,

Table of Contents

notice of class settlement, and preliminary order approving the settlement, there can be no assurance that the settlement will be approved or that objections will not be raised.

In 2004, we filed a tax appeal in the State of New York contesting a Notice of Deficiency issued by the State of New York to PlanVista Solutions, Inc. The notice involved taxes claimed to be due for the tax years ending December 31, 1999 through December 31, 2001. The amount due, including interest and penalties through September 30, 2005 is $3.1 million. We recently withdrew the tax appeal and entered into an installment payment agreement with the State of New York. Payment on the tax liability was repaid in a lump sum of $500,000 before October 30, 2005 and the remainder in equal installments that began in November 2005 with the State of New York. We entered into an agreement with a third party tax service provider to be reimbursed for 70% of the liability ultimately agreed to with the State of New York, but not to exceed $2 million. We received the $2.0 million payment from the third party in September 2005.

In December 2004, Honolulu Disposal Service, Inc. et al, referred to as HDSI, sued American Benefit Plan Administrators, Inc., referred to as ABPA, a former subsidiary of PlanVista Corporation, in the Circuit Court of the First Circuit of the State of Hawaii, alleging damages of $5,700,000 for failure to properly conduct payroll audits during the period of 1982 through 1996. The case was removed to the U.S. District Court for the District of Hawaii. Substantial discovery has taken place. ABPA has filed a motion for summary judgment seeking judgment in its favor on all claims in the case; that motion is scheduled to be heard by the federal court on March 6, 2006. If the case is not resolved via summary judgment, trial is scheduled for May 9, 2006. We are contesting the plaintiffs claims vigorously, but are unable to predict the outcome of the case or any potential liability. We tendered the defense and indemnity for the HDSI lawsuit to Hawaii Laborers Pension Trust Fund et al, referred to as HLPTF. HLPTF agreed to advance post-tender defense costs to ABPA, subject to a reservation of rights as to their contractual duties, but then filed a lawsuit for declaratory relief in June 2005, seeking a judicial determination on this issue of their duty to defend and/or indemnify ABPA in the HDSI action. Trial in that case is in the same federal court and is set for July 25, 2006. ABPA is vigorously defending the HLPTF suit and seeks from HLPTF indemnification for its defense costs and for any liability for damages, pursuant to the business contracts at issue in the HDSI litigation.

We have been named as a defendant in an action filed in December 2005 in the Eastern District of Wisconsin by Metavante Corporation. Metavante claims that our use of the name MedAvant and our logo in connection with healthcare transaction processing infringes trademark rights allegedly held by Metavante. Metavante has sought unspecified compensatory damages and injunctive relief. We believe that this action is without merit, and we are vigorously defending our use of the name MedAvant and our logo. We do not believe the proceeding will have a material adverse effect on our business, financial condition, results of operations or cash flows.

From time to time, we are party to other legal proceedings in the course of business. We, however, do not expect such other legal proceedings to have a material adverse effect on our financial condition, operating results and liquidity.

Table of Contents

Properties

Our significant offices are located as followed:

Business Segment	Location(1)	Description	Approximate Square Footage
Transaction Services	Norcross, Georgia	Corporate headquarters/operations office/data center	31,200
	Santa Ana, California	Operations office/data center	16,900
	Tampa, Florida	Operations office	8,200
	Middletown, New York	Operations office/data center	26,900
	Fort Lauderdale, Florida	Operations office	6,000
Laboratory Communication Solutions	Jeffersonville, Indiana	Operations office/warehouse	32,000

(1) All locations are leased from a third party.

We also maintain portions of our Phoenix[SM] network at a secure, third-party co-location center in Atlanta, Georgia. In addition, we also lease several mini-warehouses. Our leases and subleases generally contain renewal options and require us to pay base rent, plus property taxes, maintenance and insurance. We consider our present facilities adequate for our operations. In December 2005, we entered into a Sublease Agreement subletting out our entire Tampa office facility to a third-party beginning February 2006. We are currently searching for a significantly smaller location in Tampa to support our remaining operations there. Also, in December 2005, we signed a lease for the Fort Lauderdale location for approximately 6,000 square feet.

Available Information

Our Internet address is www.medavanthealth.com. We make available free of charge on or through our Internet website our annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Exchange Act as soon as reasonably practicable after such material was electronically filed with, or furnished to, the Securities and Exchange Commission.

Table of Contents

MANAGEMENT

Executive Officers and Directors

The following table sets forth, as of December 31, 2005, information about our executive officers and directors:

Name	Age	Position
Eric D. Arnson	34	Executive Vice President, Product Management
Cynthia Bird	51	Executive Vice President, Information Technology
William L. Bennett (1)(3)	56	Director
Christopher K. Carter	49	Executive Vice President, Sales and Account Management
Edwin M. Cooperman (2)	62	Director
Douglas J. O Dowd	40	Executive Vice President, Chief Financial Officer and Treasurer
Lonnie W. Hardin	50	Executive Vice President, Operations
Thomas E. Hodapp (1)(2)(3)	46	Director
Braden R. Kelly (2)	35	Director
John G. Lettko	48	Chief Executive Officer, President and Director
James H. McGuire	62	Director
Kevin M. McNamara	49	Chairman of the Board
Allison W. Myers	28	Executive Vice President, Human Resources
David E. Oles	45	Executive Vice President, General Counsel and Secretary
Emily J. Pietrzak	29	Executive Vice President, Marketing and Communications
Eugene R. Terry (1)(3)	67	Director

(1) Member of the Audit Committee, the Chairman of which is Mr. Bennett.

(2) Member of the Compensation Committee, the Chairman of which is Mr. Cooperman.

(3) Member of Nominating Committee, the Chairman of which is Mr. Terry.

Eric D. Arnson joined us in December 1998 in conjunction with our acquisition of Key Communications Service, Inc. Mr. Arnson served as our Vice President and General Manager of Lab Services from January 2003 to August 2005. From August 2005 through present, he has served as our Executive Vice President, Product Management. From 1998 to 2003, Mr. Arnson held a number of positions within MedAvant including Product Manager, Vice President of Corporate Marketing and Vice President of Operations for Laboratory Services. Mr. Arnson holds a BS degree in marketing from the Indiana University School of Business.

William L. Bennett was appointed as one of our directors in March 2004 in connection with our acquisition of PlanVista. Mr. Bennett passed away on January 23, 2006. From January 1998 to March 2004, Mr. Bennett was the Vice Chairman of the Board of PlanVista. Mr. Bennett served as the Chairman of the Board of PlanVista from December 1994 to December 1997 and had been a director since August 1994. From February 2000 to January 2006, Mr. Bennett was a partner and Director of Global Recruiting and Managing Director of Monitor Company Group, L.P., a strategy consulting firm and merchant bank. From May 1991 to May 2001, he was a director of Allegheny Energy, Inc., an electric utility holding company. Until March 1995, Mr. Bennett served as Chairman and Chief Executive officer of Noel Group, Inc., a publicly traded company that held controlling interests in small to medium-sized operating companies. Mr. Bennett was also a director of Sylvan, Inc., a publicly traded company that produces mushroom spawn and fresh mushrooms.

Cynthia Bird joined us in July 2005 and currently serves as our Executive Vice President, Information Technology. From July 2002 to July 2005, Ms. Bird served as a consultant to Viewpointe, a bank consortium providing paper and electronic check processing, archival and image exchange services to the financial industry, and to IBM to interface with IBM Global Operations in support of all technology changes in the Viewpointe Archive Services environment. In 2000, Ms. Bird co-founded Bridge-IT, a telecommunications and business consulting firm in Chapel Hill, North Carolina, and served as its president until 2002. From 1986 to 1998, Ms. Bird served in her final capacity as Director of Business Development at Digital Equipment Corp., where she initiated outsourcing

Table of Contents

management services, managed operational engineering, directed international technical support and network management teams, and developed and implemented its global video teleconferencing networks and international integrated broadband network backbone. Prior to joining Digital Equipment Corp., Ms. Bird held technical design and management positions with AT&T, Hartford Insurance and ROLM. Ms. Bird received a BS degree in business administration and organizational development from the University of New Hampshire.

Christopher K. Carter joined us in June 2005 and currently serves as Executive Vice President, Sales and Account Management. Prior to joining us, Mr. Carter spent 25 years directing operations, product and account management for technology and financial services companies across the globe. From March 2001 to June 2005, Mr. Carter served as Director of Image Sharing and Exchange at Viewpointe, a bank consortium providing paper and electronic check processing, archival and image exchange services to the financial industry. From November 1999 to March 2001, Mr. Carter served as Global Operations Director for Cognotec, a web-based FX trading system provider, where he established the operations division, as well as managed staff in Dublin, London, Tokyo, New York and Sydney. Mr. Carter also worked at ADP s Electronic Financial Services Group, eventually EDS Consumer Network Services, from 1987 to 1999, serving in account and product management roles, e-commerce and global business development before becoming Division Vice President and General Manager. Prior to that, Mr. Carter helped establish the Georgia Credit Union Affiliates after working at US Central Credit Union. Mr. Carter received a BBA degree in accounting from the University of Wisconsin-Madison in 1979.

Edwin M. Cooperman has served as a director of ProxyMed since July 2000. He is a principal of T.C. Solutions, a privately-held investment and financial services consulting firm. Previously, Mr. Cooperman was Chairman of the Travelers Bank Group and Executive Vice President, Travelers Group, where he was responsible for strategic marketing, the integration of Travelers brands and products, joint and cross marketing efforts and corporate identity strategies, as well as expanding the Travelers Bank Group s credit card portfolios. After joining Travelers in 1991, Mr. Cooperman became Chairman and CEO of Primerica Financial Services Group, which comprises Primerica Financial Services, Benefit Life Insurance Company and Primerica Financial Services Canada. Previous to this, Mr. Cooperman served at American Express where he became Chairman and Co-Chief Executive of Travel Related Services, North America. Mr. Cooperman is also a director of Grannum Value Mutual Fund.

Lonnie W. Hardin joined us in November 1997 in connection with our acquisition of US Health Data Interchange, Inc. Since November 2005, he has served as Executive Vice President, Operations, and from October 2000 until November 2005, he served as Senior Vice President of Payer Services. From November 1997 to October 2000, Mr. Hardin served as the Senior Vice President of Field Claims Operations. Prior to joining us, Mr. Hardin was employed by US Health Data Interchange, Inc. from 1991 through 1997, during which time he held the positions of Vice President Sales/Marketing and General Manager. Mr. Hardin is currently on the Board of Directors for the Electronic Healthcare Network Accreditation Commission and the Association for Electronic Health Care Transaction.

Thomas E. Hodapp has served as a director for us since July 2000. In 1999, Mr. Hodapp founded Access Capital Management, a private banking and management firm dedicated to providing financial and strategic advisory services to select, early stage private healthcare and information technology companies. From 1992 to 1998, Mr. Hodapp was a Managing Director for Robertson Stephens & Company, LLC, a leading international investment banking firm, overseeing the firm s Healthcare Managed Care Research Group, with a focus on the managed care, practice management and healthcare information services industries. From 1988 to 1992, he was with Montgomery Medical Ventures, a venture firm focused on the biotechnology, medical device and healthcare service fields. MMV I and II actively managed long-term investments in over 40 early stage companies, many of which the firm was involved in co-founding. Prior to that, Mr. Hodapp researched the healthcare industry as an industry analyst with Goldman, Sachs & Company, S.G. Warburg Securities and Volpe & Covington. Additionally, Mr. Hodapp has been published in a number of major financial and healthcare industry journals and publications, was a two-time selection to the Wall Street Journal Research Analyst All-Star Team, and is a frequent speaker at national healthcare investment and strategy forums.

Braden R. Kelly was appointed as a director in April 2002. Mr. Kelly is a Managing Director of General Atlantic, LLC, a leading global private equity firm providing capital for innovative companies where information technology or

intellectual property is a key driver of growth where he has been employed in various capacities since 1995. Prior to joining General Atlantic, Mr. Kelly was a member of the Mergers, Acquisitions, and Restructurings

Table of Contents

Department at Morgan Stanley & Co. He also serves as a director of Eclipsys Corporation, HEALTHvision, Inc. and Schaller Anderson, Incorporated Mr. Kelly received his BA in Finance and Business Economics from the University of Notre Dame.

John G. Lettko was appointed as our Chief Executive Officer in May 2005 and as our President in October 2005. Prior to joining us, he served as Chief Executive Officer from February 2001 to February 2005 and as Chairman of the Board from January 2002 through February 2005 for Viewpointe Archive Services, a bank consortium providing paper and electronic check processing, archival and image exchange services to the financial industry. From October 1999 to February 2001, Mr. Lettko served as president of Xpede, Inc., a software provider to bank lenders, where he led the sales, marketing, business development and investor relations functions. Prior to that, Mr. Lettko spent 10 years at Electronic Data Systems, a Global IT outsourcing company, where he managed global accounts in Asia, Europe and the Americas. Mr. Lettko also held key positions at the Progressive Companies and Fleet National Bank, where he played central roles in the formation of several regional ATM networks. Mr. Lettko holds an MBA in Finance and Management Information Systems from State University of New York at Albany and a BS from Union College.

James H. McGuire was appointed as a director in September 2005. Since 1992, Mr. McGuire has been the President of NJK Holding Corporation, a privately-held investment company that has invested in a broad spectrum of industries including financial services, health care, litigation services, certification/training, and publishing. His background includes both commercial banking and the computer and software industry. He spent 12 years with Control Data Corporation where he was a Vice President in the Peripherals Company. Mr. McGuire is a director of Digital Insight Corporation, a leading online banking provider for financial institutions, and served as Chairman of the Board from its inception in 1997 until June 1999. Mr. McGuire also has been a director since 1995 of Laureate Education Inc., a higher education company. Laureate was formerly Sylvan Learning Systems, Inc. Mr. McGuire received his BA in finance from the University of Notre Dame.

Kevin M. McNamara was appointed as a director in September 2002 and has served as Chairman of the Board since December 2004. He also served as Interim Chief Executive Officer from January 2005 to May 2005. Mr. McNamara is currently a board member of HCCA International, Inc., a healthcare management and recruitment company since April 2005. In April 2005, he became the Chief Financial Officer of Healthspring, Inc. f/k/a Newquest. Healthspring is an HMO that focuses mainly on providing health coverage to medical beneficiaries. From November 1999 until February 2001, Mr. McNamara served as Chief Executive Officer and a director of Private Business, Inc., a provider of electronic commerce solutions that helps community banks provide accounts receivable financing to their small business customers. From 1996 to 1999, Mr. McNamara served as Senior Vice President and Chief Financial Officer of Envoy. Before joining Envoy, he served as president of NaBanco Merchant Services Corporation, then one of the world s largest merchant credit card processors. Mr. McNamara currently serves on the Board of Directors of Luminex Corporation, a medical device company, and Comsys IT Partners, an information technology staffing company, as well as several private companies. He is a Certified Public Accountant and holds a BS in Accounting from Virginia Commonwealth University and a Masters in Business Administration from the University of Richmond.

Allison W. Myers joined us in June 2005 as part of a strategic task force focused on improving the company and currently serves as our Executive Vice President of Human Resources. Prior to joining us, Ms. Myers served from 2001 to 2005 for Viewpointe, a bank consortium providing electronic check processing services to the financial industry. During her tenure at Viewpointe, Ms. Myers specialized in facilities management, vendor relationships and organizational management. Ms. Myers received a BS in communications from Texas A&M University in College Station, Texas.

Douglas J. O Dowd joined us in March 2004 upon our acquisition of PlanVista Corporation. Mr. O Dowd was named our Interim Chief Financial Officer in August 2005 and as our Chief Financial Officer in October 2005. While at PlanVista, Mr. O Dowd held the position of Vice President and Controller from April 2002 until August 2005. From December 1999 to April 2002, Mr. O Dowd served as Chief Financial Officer of NexTrade Holdings, Inc., a privately held corporation that is one of six electronic communications networks approved by the United States Securities and Exchange Commission. Prior to NexTrade, Mr. O Dowd served as corporate controller from December 1996 to

December 1999 of JLM Industries, Inc., a publicly traded petrochemical manufacturer and distributor worldwide, where he led the company s initial public offering. Mr. O Dowd began his career with

Table of Contents

Deloitte and Touche, where he was a senior accountant and Certified Public Accountant. Mr. O Dowd received his MS and BS degrees in accounting from the University of Florida.

David E. Oles has served as our General Counsel and Secretary since April 2004 and was named Executive Vice President in December 2005. In January of 2006, we entered into an agreement with Mr. Oles under which he will resign his position as of January 31, 2006. Prior to joining us, Mr. Oles served as Vice President and Associate General Counsel of NDCHealth Corporation from 2000 to 2004. From 1998 through 2000, Mr. Oles engaged in the private practice of law as an associate in the Healthcare group of the law firm of Alston & Bird LLP in Atlanta, Georgia, and in the healthcare corporate group of Reed Smith Shaw and McClay, LLP from 1996 through 1998. Mr. Oles received his J.D. from Harvard Law School, and his MBA and BBA from the University of Memphis.

Emily J. Pietrzak joined us in June 2005 and currently serves as our Executive Vice President, Marketing and Communications. Prior to that time, she served as the Director of Communications from 2002 to 2005 for Viewpointe, a bank consortium providing electronic check processing and archival services to the financial industry. Before joining Viewpointe in 2002, Ms. Pietrzak served from 2001 to 2002 as the online editor for advertising agency Gear-Six, designing and launching online campaigns for the firm s largest customer. In 2001, she also served as the senior marketing consultant for The Fourth Wall, Inc., a consulting firm specializing in marketing strategy and communications. Prior to that, Ms. Pietrzak led strategic planning and marketing activities as the marketing manager for Xpede, an online mortgage application company. Ms. Pietrzak began her career at Deloitte and Touche, and she received a BS in business administration/finance from St. Mary s College in California.

Eugene R. Terry was appointed as a director in August 1995. Mr. Terry is a pharmacist and is a principal of T.C. Solutions, a privately-held investment and financial services consulting firm. Since 2004, Mr. Terry has served as a consultant for MSO Medical, a bariatric surgery management company. Until 2001, Mr. Terry was a director on the board of In-Home Health, a home healthcare company acquired by Manor Care, Inc. In 1971, Mr. Terry founded Home Nutritional Support, Inc., referred to as HNSI, one of the first companies established in the home infusion industry. In 1984, HNSI was sold to Healthdyne, Inc., and later to the W.R. Grace Group. From 1975 to 1984, Mr. Terry was also founder and Chief Executive Officer of Paramedical Specialties, Inc., a respiratory and durable medical equipment company, which was also sold to Healthdyne, Inc. Mr. Terry is a consultant and Board member in MSO and also a director of HCM, a prescription auditing firm.

Board of Directors

Our directors are elected annually at our Annual Meeting of Shareholders. Our Board of Directors currently has the following standing committees: the Audit Committee, Compensation Committee, and the Corporate Governance and Nominating Committee.

During 2005, our Audit Committee consisted of three non-employee, independent directors: William L. Bennett (Chairman), Thomas A. Hodapp and Eugene R. Terry. Mr. Bennett passed away on January 23, 2006. The Audit Committee is responsible for meeting with representatives of our independent certified registered public accountants and with representatives of senior management to review the general scope of our annual audit, matters relating to internal audit control systems and the fee charged by the independent certified registered public accountants.

Our Compensation Committee consists of three non-employee, independent directors: Edwin M. Cooperman (Chairman), Thomas E. Hodapp and Braden R. Kelly. The Compensation Committee is responsible for making recommendations to the Board on the annual compensation for all officers, and employees, including salaries, stock options and other consideration, if any. The Compensation Committee is also responsible for granting stock options to be made under our existing plans.

During 2005, the Corporate Governance and Nominating Committee consisted of three non-employee, independent directors: Eugene R. Terry (Chairman), William L. Bennett and Thomas E. Hodapp. Mr. Bennett passed away on January 23, 2006. The Corporate Governance and Nominating Committee is responsible for providing assistance to our Board of Directors to determine the size, functions and needs of the Board of Directors, and the selection of candidates for election to the Board of Directors, including identifying, as necessary, new candidates who are qualified to serve as our directors and recommending to the Board of Directors, the candidates for election to the Board of Directors. In addition, the Corporate Governance and Nominating Committee has responsibility for overseeing the selection, retention and conduct of our executive

55

Table of Contents

officers. Finally, the Corporate Governance and Nominating Committee has overall responsibility for ensuring our appropriate corporate governance. The Corporate Governance and Nominating Committee will also consider director candidates recommended by shareholders.

Compensation Committee Interlocks and Insider Participation

None of the members of the Compensation Committee was an officer (or former officer) or employee of ours or any of our subsidiaries;

None of the members of the Compensation Committee had any relationship requiring disclosure under any paragraph of Item 404 of Regulation S-K;

None of the our executive officers served on the compensation committee (or another board committee with similar functions) of any entity where one of that entity s executive officers served on our Compensation Committee;

None of our executive officers was a director of another entity where one of that entity s executive officers served on our Compensation Committee; and

None of the our executive officers served on the compensation committee (or another board committee with similar functions) of another entity where one of that entity s executive officers served as a director on our Board.

Director Compensation

Effective February 17, 2005, each non-employee director shall receive cash compensation in the amount of $5,000 per quarter for attending each regularly scheduled general Board of Directors meeting. Additionally, all directors are reimbursed for reasonable expenses incurred in attending board meetings. Previously, non-employee directors were compensated with stock options for their services as directors as follows: each non-employee director was granted 15,000 stock options upon his or her initial appointment or election to the Board of Directors by the shareholders, with such grant vesting equally over the following three years. On each subsequent election by the shareholders, each non-employee director received an additional 5,000 share stock option grant which vested immediately. Additionally, each non-employee director receives an annual 2,500 share stock option grant for each subcommittee membership. Such subcommittee grants vest on a prorata basis (based on four projected subcommittee meetings per election year) as determined by the attendance of the director at each subcommittee meeting, but in any event, after three years. For the 2003-2004 election year, options to purchase a total of 30,000 and 15,000 options at an exercise price of $10.63 were granted to compensate the directors upon re-election to the board and participation in sub-committees, respectively, pursuant to the above guidelines. Of the sub-committee amount, 11,250 stock options vested as of December 31, 2003 and the remaining 3,750 stock options vested in 2004. For the 2004-2005 election year, options to purchase a total of 35,000 and 15,000 options at an exercise price of $20.00 were granted to compensate the directors upon re-election to the board and participation in sub-committees, respectively, pursuant to the above guidelines. Of the sub-committee amount, all of the 15,000 stock options were vested by December 31, 2004.

In December 2004, stock options to purchase 75,000 shares of our Common Stock at an exercise price of $7.10 per share were granted to Kevin M. McNamara in connection with his consulting agreement with us. Such options expire in ten years and vest equally over the 12 months following December, 2004 at the rate of 6,250 per month. In January 2005, Mr. McNamara was granted stock options to purchase another 25,000 shares of our Common Stock at $9.87 per share in his capacity as Chairman of the Board. Such options expire in ten years and vest equally over the twelve months following January 2005 at the rate of 2,083 per month. In May 2005, we terminated our consulting agreement with Mr. McNamara which accelerated his vesting of options under the Agreement.

Table of Contents

Executive compensation

The following table sets forth the compensation paid during the past three fiscal years to our Chief Executive Officers and our other four most highly compensated executive officers during fiscal year 2005 with annual compensation over $100,000 for such years (the Named Executive Officers):

Summary Compensation Table

		Annual Compensation			Long-Term Compensation Awards		Payouts	
Name and Principal Position	Year	Salary ($)	Bonus ($)	Other Annual Compensation ($)	Restricted Stock Award(s) ($)	Securities Underlying Options/ SARs (#)	LTIP Payouts ($)	All Other Compen-sation ($)
Kevin M. McNamara	2005			290,000		25,000		
Chairman and Interim	2004			30,000(1)		82,500(1)		
Chief Executive Officer (1)	2003					17,500		
Michael K. Hoover	2005	40,757						
Chairman and Chief	2004	275,000	15,000(3)	46,601(4)				
Executive Officer (1)	2003	222,115				125,000		
John G. Lettko								
Chief Executive Officer (11)	2005	244,615				600,000		
Douglas J. O Dowd								
Chief Financial Officer (12)	2005	120,560	10,000			1,685		
David E. Oles	2005	175,071				19,000		
General Counsel and Secretary	2004	165,000				19,000		
Gregory J. Eisenhauer	2005	248,450						
EVP and Chief	2004	225,000	25,000			18,000		
Financial Officer (7)	2003	8,654				100,000		
John Paul Guinan	2005	223,139	10,000					
EVP and Chief	2004	185,000	10,000(2)					
Technology	2003	186,846	2,500(2)					

Officer(9)					
Nancy J. Ham	2005	254,445	10,000		
President and	2004	224,231	22,500(2)(3)		
Chief Operating Officer(10)	2003	198,846	4,688(2)	50,765(5)	50,000
Lonnie W. Hardin	2005	196,923	10,000		34,528
EVP, Business	2004	185,000	10,000(2)		
Operations	2003	184,246	8,950(2)		

(1) Mr. Hoover retired as Chairman of the Board in December 2004 and as Chief Executive Officer in January 2005. Mr. McNamara, was appointed to fill these positions at those times. Concurrent with his appointment as Chairman, Mr. McNamara entered into a consulting agreement with us. Pursuant to the consulting agreement, Mr. McNamara was entitled to receive cash compensation of $30,000 per month and was granted a ten-year option to purchase 75,000 shares of our common stock at $7.10 per share. Such options vested 100% at the

appointment of Mr. Lettko as Chief Executive Officer in May 2005.

Table of Contents

(2) Earned in current fiscal year but paid in following fiscal year.

(3) Includes a bonus of $12,500 earned and paid in 2004 for the PlanVista acquisition.

(4) Consists of reimbursement of relocation expenses of $46,601, including a tax reimbursement of $16,054 in 2004.

(5) Consists of reimbursement of relocation expenses of $50,765, including a tax reimbursement of $16,753 in 2003; and reimbursement of relocation expenses of $9,461, including tax reimbursement of $3,122 in 2002.

(6) Consists of reimbursement of living expenses for Florida housing, including tax reimbursements of $7,020 in

2002.

(7) Mr. Eisenhauer joined the Company on December 8, 2003. As part of his employment agreement dated December 8, 2003, Mr. Eisenhauer received an annual salary of $225,000, an annual bonus of up to 50% of his base salary and a guaranteed 2004 bonus of $25,000 which was paid in January 2004. Additionally, as part of his employment, Mr. Eisenhauer received a ten-year option to purchase up to 100,000 shares of common stock at $16.01 per share. Such options vest over a three year period. Mr. Eisenhauer received an additional grant of a ten-year option to purchase up to 18,000 shares of our common stock at $16.53. Mr. Eisenhauer left the Company in August 2005.

(8) Includes stock options cancelled and reissued as follows: 13,333 options for Mr. Guinan and 1,434 options for Mr. Hardin.

(9) Mr. Guinan left employment from the Company in September 2005

(10) Ms. Ham left employment from the Company in June 2005.

(11) Mr. Lettko became Chief Executive Officer in May 2005 and his contracted annual salary is $400,000.

(12) Mr. O Dowd was named Interim Chief Financial Officer on August 15, 2005 and appointed Chief Financial Officer on October 27, 2005.

The following table provides information on stock option grants during fiscal year 2005 to each of the Named Executive

Officers:

Option/SAR Grants in Last Fiscal Year

	Individual Grants				Potential Realizable Value at Assumed Annual Rates of Stock Price Appreciation for Option Term*	
Name	# of Securities Underlying Options/ SARs Granted	% of Total Options/SARs Granted To Employee In Fiscal Year	Exercise or Base Price	Expiration Date	5%	10%
Kevin M. McNamara	25,000	2.6%	$ 9.87	1/18/2015	$ 155,179	$ 393,255
John G. Lettko	600,000	63.6%	$ 6.45	5/10/2015	$2,433,822	$6,167,783
Douglas J. O Dowd	1,685		$ 3.55	11/17/2015	$ 3,761	$ 9,533
Lonnie W. Hardin	34,527	3.6%	$ 3.55	11/17/2015	$ 77,084	$ 195,346
David E. Oles	19,000	1.9%	$ 3.55	11/17/2015	$ 42,419	$ 107,498
Michael K. Hoover			$		$	$
Nancy J. Ham	103,751	2.16%	$ 15.90	10/09/2013	$	$
Gregory J. Eisenhauer			$		$	$
John Paul Guinan			$		$	$

* The assumed annual rates of stock price appreciation are required disclosures, and are not intended to forecast future stock appreciation.

Table of Contents

The following table sets forth certain information concerning unexercised options held by each of the Named Executive Officers:

Aggregated Option/SAR Exercises in Last Fiscal Year and FY-End Options/SAR Values

Name	# of Shares Acquired on Exercise	$ Value Realized	Number of Securities Underlying Unexercised Options/SARs at FY-End (#)		Value of Unexercised In-the-Money Options/SARs at FY-End ($)**	
			Exercisable	Unexercisable	Exercisable	Unexercisable
Kevin M. McNamara			136,250	5,625	$	$
John G. Lettko			75,833	524,167	$	$
Douglas J. O Dowd			707	2,663	$	$ 859
Nancy J. Ham			99,168		$	$
Lonnie W. Hardin			29,015	43,367	$	$ 17,609
Michael K. Hoover					$	$
David E. Oles			1,334	17,666	$	$
Gregory J. Eisenhauer					$	$
John Paul Guinan					$	$

** Year-end values for unexercised in-the-money options represent the positive spread between the exercise price of such options and the fiscal year-end market value of the common stock, which was $4.06 on December 31, 2005.

Long Term Incentive Plan Awards

There were no awards made to Named Executive Officers in the last completed fiscal year under any long-term incentive plan for performance to occur over a period longer than one fiscal year. We do not have any defined benefit or actuarial plans for our employees.

Ten-Year Option/SAR Repricings

There were no option repricings for Named Executive Officers during the year ended December 31, 2005.

Table of Contents

Change of Control

In February 2005, the Compensation Committee of our Board of Directors agreed to authorize bonuses for members of executive and senior management in the event of a change in control of our company. These bonuses total $1.5 million in the aggregate. Under the guidelines approved by the Compensation Committee, such bonuses are payable in cash and the recipient must be an active employee at the time of such event.

Equity Compensation Plans

We have various stock option plans for employees, directors and outside consultants, under which both incentive stock options and non-qualified options may be issued. Under such plans, options to purchase up to 2,031,017 shares of common stock may be granted. Options may be granted at prices equal to the fair market value at the date of grant, except that incentive stock options granted to persons owning more than 10% of the outstanding voting power must be granted at 110% of the fair market value at the date of grant. At the Company s Special Meeting of Shareholders held on March 1, 2004 to approve the Company s acquisition of PlanVista, the shareholders approved an amendment to the 2002 Stock Option Plan to increase the total number of shares available for issuance from 600,000 to 1,350,000 shares that may be issued to employees, officers and directors. In addition, as of December 31, 2003, options for the purchase of 400,407 shares to newly-hired employees remain outstanding. Stock options issued by the Company generally vest within three or four years, and expire up to ten years from the date granted. See Note 14 to the Consolidated Financial Statements and related notes for more information on our equity compensation plans.

The following table sets forth information regarding our compensation plans under which equity securities are authorized for issuance as of December 31, 2005:

Equity Compensation

Plan Category	Number of securities to be issued upon exercise of outstanding options, warrants and rights	Weighted-average exercise price of outstanding options, warrants and rights	Number of securities remaining available for future issuance under equity compensation plans
Equity compensation plans approved by security holders	1,903,579	$ 9.44	86,318
Equity compensation plans not approved by security holders (1)	400,406	$21.52	
TOTAL	2,303,985	$11.54	86,318

(1) The Company maintains a stock option plan to grant stock options to newly-hired employees. Such plan was not required to be approved by the shareholders of the Company. Since January 2002, no additional grants of options have been made from

this plan. Any grants to newly-hired employees since January 2002 have been made from plans approved by our shareholders.

Employment Agreements with the Named Executive Officers

In December 2004, we entered into an independent contractor agreement with Mr. McNamara. The agreement was on a month-to-month basis for a minimum of six months and shall be automatically renewed unless either party gives thirty days written notice of non-renewal. Under this agreement, Mr. McNamara was paid a cash fee of $30,000 per month. Additionally, in conjunction with this agreement, Mr. McNamara received ten-year options to purchase 75,000 shares of our common stock at an exercise price of $7.10 per share. Such options vested at the rate of 6,250 per month but could be accelerated to fully vest upon a change in control of the Company or if the independent contractor agreement is terminated within the first six months for any reason other than breach of contract. In January 2005, in conjunction with Mr. McNamara s appointment as Chairman of the Board, he is also paid a cash fee of $10,000 per month and received ten-year options to purchase an additional 25,000 shares of our common stock at an exercise price of $9.87 per share. These options vest at the rate of 2,083 per month and could be accelerated to vest in the case of a change in control of our Company. In May 2005, we terminated our

Table of Contents

consulting agreement with Mr. McNamara and this triggered the acceleration of the vesting of his stock options. As a result, we recorded a charge of $86,600 in May 2005.

In July 2000, we entered into an employment agreement with Mr. Hoover. The agreement was for a three-year term and automatically extended from year to year thereafter unless terminated by us upon 90 days written notice or by him upon 30 days written notice prior to the end of the initial term or any extension. As of December 31, 2004, Mr. Hoover received an annual base salary of $275,000 (effective January 1, 2004, as approved by the Compensation Committee in October 2003) and was entitled to such bonuses as may be awarded from time to time and to participate in any stock option plans that we may now have. In addition, the agreement contains confidentiality and non-competition covenants. In December 2004, Mr. Hoover stepped-down as Chairman of the Board and in January 2005, he retired as chief executive officer. In accordance with the terms of termination of his employment agreement, Mr. Hoover received no severance or any other additional compensation upon his separation from the Company.

In December 2003, the Company entered into an employment agreement with Mr. Eisenhauer. The agreement is for a three-year term and automatically extends from year to year thereafter unless terminated by us upon 90 days written notice or by him upon 30 days written notice prior to the end of the initial term or any extension. Under this agreement, Mr. Eisenhauer received an annual base salary of $225,000, was entitled to earn an annual bonus of up to 50% of his base salary as well as bonuses that may be awarded from time to time, and was paid a guaranteed 2004 bonus of $25,000 in January 2004. Additionally, as part of his employment agreement, Mr. Eisenhauer received a ten-year option to purchase up to 100,000 shares of Common Stock at $16.01 per share. Such options vested over a three-year period. Mr. Eisenhauer was eligible to participate in any stock option plans that we had or in the future developed. If terminated for cause, he would have been entitled to base salary earned, and he would retain all vested stock options. If he were terminated without cause, he was entitled to receive an amount equal to his base salary plus bonus, if any, for six months and the continuation of health insurance for three months following termination, plus any unvested options shall vest. In addition, the agreement contained confidentiality and non-competition covenants. In February 2005, Mr. Eisenhauer s employment agreement was amended to provide for 90-days prior written notice if he is terminated without cause. Under guidelines approved by our Compensation Committee in February 2005 to authorize bonuses for members of executive and senior management in the event of a change in control of our Company, the amount of the bonus for Mr. Eisenhauer would be $100,000, payable in cash. In order to earn such bonus, he must be an active employee at the time of such change of control. In August of 2005, the Company entered into a separation agreement with Mr. Eisenhauer under which he will be paid $100,000 severance in bi-weekly increments based on his usual payroll amount. In addition, all of Mr. Eisenhauer s Company stock options expired on August 20, 2005.

In October 2000, we entered into an employment agreement with Ms. Ham. The agreement was for a three-year term and automatically extended from year to year thereafter unless terminated by us upon 90 days written notice or by her upon 30 days written notice prior to the end of the initial term or any extension. Ms. Ham received an annual base salary of $225,000 and was entitled to such bonuses as may be awarded from time to time and to participate in any stock option plans that we may now have or in the future develop. She could have been terminated for cause as defined in her agreement. If terminated for cause, she would have been entitled to base salary earned, and she could retain all vested stock options. If, upon 90 days prior written notice, she is terminated without cause, she could be entitled to receive an amount equal to her base salary plus bonus, if any, and continuation of health insurance for six months following termination, plus any unvested options shall vest. In addition, the agreement contained confidentiality and non-competition covenants. Under guidelines approved by our Compensation Committee in February 2005 to authorize bonuses for members of executive and senior management in the event of a change in control of our Company, the amount of the bonus for Ms. Ham was $500,000, payable in cash. In order to earn such bonus, she must be an active employee at the time of such change of control. In June of 2005, the Company entered into a separation agreement with Ms. Ham under which she will be paid a monthly severance of $18,750, and receive continued Company benefits, for twelve (12) months. In addition, Ms. Ham was granted 18 months in which to exercise any vested stock options.

In December 1995, we entered into an employment agreement with Mr. Guinan, which is automatically extended from year to year unless terminated by either party upon 60 days written notice. Mr. Guinan received an annual base salary of $195,000 (effective January 1, 2005, as approved by our Compensation Committee in February 2005) and was entitled to such bonuses as may be awarded from time to time by the Board of Directors and to participate in any stock option plans that we may now have or in the future develop. Mr. Guinan could be terminated for cause as defined in the agreement. If he was terminated for cause, he would be entitled to base salary earned, and he would retain all vested stock options. If he was terminated without cause, then he would have been entitled to receive an amount equal to his base salary and bonus, if any, and continuation of health insurance for six months following termination, plus any unvested options shall vest. In addition, the agreement contained confidentiality and non-competition covenants. Under guidelines approved by our Compensation Committee in February 2005 to authorized bonuses for members of executive and senior management in the event of a change in control of our company, the amount of the bonus for Mr. Guinan would have been $100,000, payable in cash. In order to earn such bonus, he must be an active employee at the time of such change of control. In August of 2005, the Company entered into a Separation Agreement with Mr. Guinan under which he will be paid six months severance in bi-weekly increments based on his usual payroll amounts. In addition, Mr. Guinan received continued Company benefits for the same six month period.

Table of Contents

In March 2001, we entered into an employment agreement with Mr. Hardin. The agreement is for a three-year term and automatically extends from year to year thereafter unless terminated by us upon 90 days written notice or by him upon 30 days written notice prior to the end of the initial term or any extension. Mr. Hardin currently receives an annual base salary of $195,000 (effective January 1, 2005, as approved by our Compensation Committee in February 2005), and is entitled to such bonuses as may be awarded from time to time and to participate in any stock option plans that we may now have or in the future develop. He may be terminated for cause as defined in his agreement. If terminated for cause, he will be entitled to base salary earned, and he will retain all vested stock options. If he is terminated without cause, he will be entitled to receive an amount equal to his base salary plus bonus, if any, and continuation of health insurance for six months following termination, plus any unvested options shall vest. In addition, the agreement contains confidentiality and non-competition covenants. Under guidelines approved by our Compensation Committee in February 2005 to authorize bonuses for members of executive and senior management in the event of a change in control of our company, the amount of the bonus for Mr. Hardin will be $100,000, payable in cash. In order to earn such bonus, he must be an active employee at the time of such change of control. In addition, upon a change in control all unvested options held by Mr. Hardin will accelerate and become automatically vested.

In May 2005, we entered into an employment agreement with Mr. Lettko. The agreement is for a four-year term and automatically extends from year to year thereafter unless either party issues notice of non-renewal 90 days prior to the end of the initial term or any extension. Mr. Lettko currently receives an annual base salary of $400,000 and may receive up an additional $400,000 as an annual bonus. At the time of his employment, Mr. Lettko received 400,000 stock options with an exercise price of $6.45 that vest pro rata over four (4) years. Mr. Lettko also received 200,000 performance based options that vest in four increments when the Company s share price reaches each of $15, $20, $25, and $30. Mr. Lettko is entitled to any Company bonuses that may be awarded from time to time and to participate in any stock option plans that we may now have or in the future develop. He may be terminated for cause as defined in his agreement. If terminated for cause, he will be entitled to base salary earned, and he will retain all vested stock options. If he is terminated without cause, he will be entitled to receive an amount equal to his base annual salary plus bonus, if any, and continuation of health insurance for 12 months following termination. Upon without cause termination, all time vested options will continue to vest for 12 months, plus one half of all performance based options will vest immediately. In addition, the agreement contains confidentiality and non-competition covenants upon change in control all unvested options held by Mr. Lettko will accelerate and become automatically vested.

In April 2004, we entered into an employment agreement with Mr. Oles. The agreement is for a three (3) year term and automatically extends from year to year thereafter unless either party issues notice of non-renewal 90 days prior to the end of the initial term or any extension. Mr. Oles currently receives an annual base salary of $175,000, and may receive up to 25% of base salary as an annual bonus. Mr. Oles may be terminated for cause as defined in his agreement. If terminated for cause, he will be entitled to base salary earned, and he will retain all vested stock options. If he is terminated without cause, he will be entitled to receive an amount equal to his base monthly salary for six (6) months plus bonus, if any, and continuation of health insurance for 6 months following termination. Upon termination without cause all unvested options will vest immediately. In addition, the agreement contains confidentiality and non-competition covenants. In January of 2006, we entered into an agreement with Mr. Oles under which he will resign his position as of January 31, 2006. Mr. Oles will receive four (4) months severance and continuation of health insurance and other benefits for 6 months following termination.

Table of Contents

RELATED PARTY TRANSACTIONS

In March 2001, Mr. Guinan entered into an uncollateralized promissory note for $45,400 for amounts previously borrowed from us. The promissory note called for minimum bi-weekly payments of $350 deducted directly from Mr. Guinan s payroll until the note is paid in full on or before February 2006. The note is non-interest bearing but interest is imputed annually based on the Internal Revenue Service Applicable Federal Rate at the time the note was originated (4.98%). Under terms of the promissory note, if Mr. Guinan is terminated without cause, the note is due in full after nine months from the date of termination as long as the scheduled bi-weekly payments continue to be made. As of September 30, 2005, the unpaid principal balance of the note is approximately $1,000. In August of 2005, the Company entered into a separation agreement with Mr. Guinan under which he will be paid six months of severance in biweekly increments based on his usual payroll amount. In addition, Mr. Guinan received continued Company benefits for the same six month period.

Michael S. Falk, a former non-employee director of ours, was the beneficial owner of the PlanVista Series C Preferred Stock owned by PVC Funding Partners, LLC. He is also a controlling owner of Commonwealth Associates Group Holdings, LLC, which is the managing member of PVC Funding Partners, LLC, which owned 96% of the outstanding PlanVista series C preferred stock and represented 57.9% of the combined voting power of the common stock and series C preferred stock of PlanVista. Commonwealth Associates Group Holdings, LLC acted as one of PlanVista s investment advisors in connection with the merger and received upon consummation of the merger an investment advisory fee of approximately $1.7 million. Mr. Falk is the beneficial owner of approximately 287,720 shares that were issued in connection with the private equity offering we consummated in March 2004. Additionally, one former senior executive of ours had an immaterial ownership interest in PlanVista.

William L. Bennett, a former director of PlanVista, became a director of ours following consummation of the merger with PlanVista. PlanVista was obligated to Mr. Bennett under a promissory note in the principal amount of $250,000 which had a maturity date of December 1, 2004. The note bore interest at a rate of prime plus 4.0% per annum, but payment of principal and interest was subordinated and deferred until all senior obligations were paid. The promissory note was paid in full in May 2005.

In conjunction with our acquisition of PlanVista, we assumed and guaranteed a $20.4 million secured obligation to PVC Funding Partners, LLC an owner of approximately 20% of our outstanding Common Stock. This secured obligation was repaid in full on April 18, 2005.

On December 7, 2005, the Company and certain of its wholly-owned subsidiaries, entered into a security and purchase agreement (the Loan Agreement) with Laurus Master Fund, Ltd. (Laurus) to provide up to $20 million in financing to the Company. The proceeds were used to repay the assets based facility noted above.

Under the terms of the Loan Agreement, Laurus will extend financing to the Company in the form of a $5 million secured term loan (the Term Loan) and a $15 million secured revolving credit facility (the Revolving Credit Facility). The Term Loan has a stated term of five (5) years and will accrue interest at Prime plus 2%, subject to a minimum interest rate of 8%. The Term Loan is payable in equal monthly principal installments of approximately $89,300 until the maturity date on December 6, 2010. The Revolving Credit Facility has a stated term of three (3) years and will accrue interest at the 90 day LIBOR rate plus 5%, subject to a minimum interest rate of 7%, and a maturity date of December 6, 2008. Additionally, in connection with the Loan Agreement, the Company issued 500,000 shares of its Common Stock, par value $0.001 per share (the Closing Shares) to Laurus.

The Company has granted Laurus a first priority security interest in substantially all of the Company s present and future tangible and intangible assets (including all intellectual property) to secure the Company s obligations under the Loan Agreement. The Loan Agreement contains various customary representations and warranties of the Company as well as customary affirmative and negative covenants, including, without limitation, limitations on liens of property, maintaining specific forms of accounting and record maintenance, and limiting the incurrence of additional debt. The Loan Agreement does not contain restrictive covenants regarding minimum earning requirements, historical earning levels, fixed charge coverage, or working capital requirements.

Table of Contents

PRINCIPAL SHAREHOLDERS

The following table sets forth information known to us with respect to the beneficial ownership of our common stock as of December 31, 2005 and as adjusted to reflect the sale of common stock offered hereby by:

- each shareholder known by us to own beneficially more than five percent of our common stock;
- each of the named executive officers listed in the Summary Compensation Table on page 57;
- each of our directors; and
- all of our directors and the executive officers as a group.

We have determined beneficial ownership in accordance with the rules of the Securities and Exchange Commission. In computing the number of shares beneficially owned by a person and the percentage ownership of that person, shares of common stock subject to options or warrants held by that person that are currently exercisable or exercisable within 60 days of December 31, 2005 are deemed outstanding, but are not deemed outstanding for computing the percentage ownership of any other person. To our knowledge, except as set forth in the footnotes to this table and subject to applicable community property laws, each person named in the table has sole voting and investment power with respect to the shares set forth opposite such person s name. Except as otherwise indicated, the address of each of the persons in this table is 1854 Shackleford Court, Suite 200, Norcross, Georgia 30093.

Name and Address (1)	# of Shares (2)	% of Class
William L. Bennett (3)	25,518	*
Edwin M. Cooperman (4)	51,499	*
Gregory J. Eisenhauer, CFA (5)	0.00	*
Michael S. Falk (6)	2,639,006	20.9%
John Paul Guinan (7)	0.00	*
Nancy J. Ham (8)	103,751	2.16%
Lonnie W. Hardin (9)	29,015	*
Thomas E. Hodapp (10)	45,358	*
Michael K. Hoover (11)	143,303	3.8%
Braden R. Kelly (12)	3,420,761	28.0%
Jeffrey L. Markle (13)	22,144	*
Kevin M. McNamara (14)	136,250	2.67%
Eugene R. Terry (15)	42,291	*
John G. Lettko (16)	153,353	4.0%
Douglas J. O Dowd (17)	2,663	*

David E. Oles (18)	20,384	*

Table of Contents

Name and Address (1)	# of Shares (2)	% of Class
General Atlantic, LLC(12)	3,381,802	26.8%
PVC Funding Partners, LLC(6)(19) 830 Third Avenue New York, NY 10022	2,080,115	16.5%
FMR Corporation (20) 1 Federal Street Boston, MA 02110	425,400	3.345%
All directors and officers As a group (16 persons)(21)	6,383,815	48.3%

* Less than 1%

(1) The address for each person, unless otherwise noted, is 1854 Shackleford Court, Suite 200, Norcross, Georgia 30093.

(2) In accordance with Rule 13d-3 of the Securities Exchange Act of 1934 (the Exchange Act), shares that are not outstanding, but that are subject to options, warrants, rights or conversion privileges exercisable within 60 days from December 31, 2005, have been deemed to be outstanding for the purpose of computing the

percentage of outstanding shares owned by the individual having such right, but have not been deemed outstanding for the purpose of computing the percentage for any other person.

(3) Represents 20,153 shares held of record, including 99 shares held in trust for Mr. Bennett s children and 5,365 shares issuable upon the exercise of stock options exercisable within 60 days.

(4) Includes 9,000 shares held of record and 42,499 shares issuable upon the exercise of stock options exercisable within 60 days.

(5) Includes 33,334 shares issuable upon the exercise of stock options exercisable within 60 days, which has expired.

(6)

Includes 2,615,047 shares held of record by Michael Falk, family members, family trusts and related parties and 23,959 shares issuable upon the exercise of stock options and warrants exercisable within 60 days. The shares hold of record include (i) 19,431 shared held of record by Commonwealth Associates, LP for which Mr. Falk is a control person; (ii) 6,741 shares held of record by ComVest Venture Partners, LP for which Mr. Falk is a managing member; (iii) 112,281 shares held of record by ComVest Venture Partners, LP for which Mr. Falk is a managing partner; (iv) 248,446 shares held of record and 2,822 shares issuable upon the exercise of

warrants exercisable within 60 days by Commonwealth Liquidation, LLC for which Mr. Falk is a controlling member; (v) 530 shares held of record by Commonwealth Associates Group Holding, LLC of which Mr. Falk is the chairman and a principal member; and (vi) 2,080,115 shares held of record by PVC Funding Partners, LLC which is managed by Commonwealth Associates, LP and ComVest Venture Partners, LLC. Mr. Falk disclaims beneficial ownership in all of these affiliated entities to the extent owned by third-party investors.

(7) Includes 67 shares held of record and 43,865 shares issuable upon the exercise of stock options exercisable

within 60 days, which has expired.

(8) Includes 4,583 shares held of record and 99,168 shares issuable upon the exercise of stock options exercisable within 60 days.

(9) Includes 29,015 shares issuable upon exercise of stock options exercisable within 60 days.

(10) Includes 3,067 shares held of record and 42,291 shares issuable upon exercise of stock options exercisable within 60 days.

(11) Includes 143,303 shares held of record and 416,121 shares issuable upon exercise of stock options exercisable within 60 days.

(12) Includes 38,959 shares issuable upon exercise of stock options exercisable in 60 days by Mr. Kelly. Additionally, includes the following shares

of common stock held by various General Atlantic entities: (i) 1,166,184 shares owned by General Atlantic Partners 77, L.P.; (ii) 1,741,258 shares owned by General Atlantic partners 74, L.P.; (iii) 236,441 shares owned by GAP Coinvestments Partners II, L.P.; (iv) 63,943 shares owned by GAP Coinvestments III, LLC; (v) 15,930 shares owned by GAP Coinvestments IV, LLC; (vi) 4,782 shares owned by GAPCO Management; and 153,264 shares owned by Gapstar, LLC.

Table of Contents

(13) Includes 22,144 shares held of record.

(14) Includes 136,250 shares issuable upon exercise of stock options exercisable within 60 days.

(15) Includes 42,291 shares issuable upon exercise of stock options exercisable within 60 days.

(16) Includes 77,520 shares held of record and 75,833 stock options exercisable within 60 days.

(17) Includes 1,685 shares held of record and 978 stock options exercisable within 60 days.

(18) Includes 50 shares held of record and 20,334 stock options exercisable within 60 days.

(19) Includes 2,080,115 shares held of record as reported under Form 13D filed on March 2,

2004.

(20) Includes 425,400 shares held of record as reported under Form 13G/A filed on October 11, 2005

(21) Includes 6,383,815 shares held of record by the officers and directors and their related parties and 930,288 shares issuable upon exercise of stock options and warrants exercisable in 60 days.

Table of Contents

SELLING SHAREHOLDERS

The 1,231,322 shares of Common Stock covered by this prospectus were acquired by the Selling Shareholders in certain privately negotiated transactions as described below.

Five hundred thousand of the shares of our Common Stock that may be sold from time to time pursuant to this prospectus are being offered by Laurus Master Fund, Ltd. (Laurus). On December 7, 2005, we entered into a loan transaction with Laurus pursuant to which Laurus extended $20.0 million in financing to us in the form of a $5.0 million secured term loan and a $15.0 million secured revolving credit facility. In connection with the loan agreement, we issued 500,000 shares of our Common Stock to Laurus, which shares are being offered pursuant to this prospectus.

The remaining 731,322 shares of Common Stock may be offered by the founders of MedUnite, Inc: Aetna, Anthem, CIGNA, Health Net, Oxford Health Plans, PacifiCare Health Systems, Wellpoint Health Network, and NDCHealth Corporation upon the conversion of certain 4% convertible promissory notes issued by us in connection with our acquisition of all of the outstanding stock of MedUnite in December 2002. The convertible promissory notes (now currently payable at a maturity value of $13.1 million after a claim set off against the escrow in December 2003) are payable in full on December 31, 2008 and are convertible into an aggregate of 716,968 shares (originally 731,322 shares before the claim set off) of our Common Stock if our revenues resulting from business with the former MedUnite owners exceed certain thresholds over a three and one half year period from the date of acquisition. Upon the conversion of all of the $13.1 million promissory notes held by the founders of MedUnite, the entire outstanding indebtedness associated with the acquisition will be extinguished without further payment by us.

Beneficial ownership is determined in accordance with the rules of the Securities and Exchange Commission. In computing the number of shares beneficially owned by a person and the percentage ownership of that person, shares of common stock subject to options or warrants held by that person that are currently exercisable or exercisable within 60 days of December 31, 2005 are deemed outstanding, but are not deemed outstanding for computing the percentage ownership of any other person.

The following table sets forth certain information with respect to the beneficial ownership of our common stock as of December 31, 2005 for all of the Selling Shareholders.

	Shares Beneficially Owned Prior to Offering Common Stock			Shares Beneficially Owned After Offering Common Stock	
Name of Beneficial Owner	**Shares**	**%**	**Shares Being Offered**	**Shares**	**%**
Selling Shareholders:					
Laurus Master Fund, Ltd.	500,000	3.8%	500,000	500.000	3.8%
Aetna, Inc.	0		86,584	86,584	0.7%
Anthem Insurance Companies, Inc.	0		86,441	86,441	0.7%
CIGNA Health Corporation	0		86,547	86,547	0.7%
Health Net, Inc.	0		86,488	86,488	0.7%
NDCHealth Corporation	0		128,446	128,446	1.0%
Oxford Health Plans, Inc.	0		78,212	78,212	0.6%
PacifiCare Health Systems, Inc.	0		77,784	77,784	0.6%
Wellpoint Health Network, Inc.	0		86,466	86,466	0.7%

The preceding table represents the holding by the Selling Shareholders based upon our best upon our best knowledge and assumes that all Selling Shareholders eligible to convert their notes payable to shares will do so prior

Table of Contents

to termination of this offering. The Selling Shareholders identified above may have sold, transferred or otherwise disposed of in transactions exempt from the requirements of the Securities Act, all or a portion of their shares of our common stock since the date as of which the information in the preceding tables is presented. Information concerning the Selling Shareholders may change from time to time, which changed information will be set forth in supplements to this prospectus if and when necessary. Because the Selling Shareholders may not convert all of their notes to shares at any given time, or offer all or some of the shares of our Common Stock that they hold, we cannot give an estimate as to the amount of Common Stock that will be held by the Selling Shareholders upon the termination of this offering. See Plan of Distribution

Table of Contents

DESCRIPTION OF CAPITAL STOCK

As of the date of this prospectus, our authorized capital stock consists of 30,000,000 shares of Common Stock, par value $.001 per share, and 2,000,000 shares of Preferred Stock, par value $.01 per share, of which 445,000 shares have been designated as Series A Preferred Stock (130,000 shares designated and issued), Series B Preferred Stock (15,000 shares designated and issued) or Series C Preferred Stock (300,000 shares designated and 253,265 shares issued) with currently no Series A or B preferred shares outstanding and only 2,000 Series C preferred shares outstanding, convertible into 13,333 shares of Common Stock.

The following description summarizes the terms of our Common Stock and Series C Preferred Stock only and does not purport to be complete. Such description is subject to and qualified by the actual agreements relating to our Series C Preferred Stock and our amended and restated articles of incorporation and by-laws, all of which have been filed with the SEC, and by applicable law.

Common Stock

The issued and outstanding shares of Common Stock are validly issued, fully paid and non-assessable. All shares of Common Stock have equal voting rights and, when validly issued and outstanding, have one vote per share in all matters to be voted upon by the shareholders. Cumulative voting in the election of directors is not allowed, which means that the holders of more than 50% of the outstanding shares can elect all the directors if they choose to do so and, in such event, the holders of the remaining shares will not be able to elect any directors. The shares have no preemptive, subscription, conversion or redemption rights. Upon liquidation, dissolution or winding-up of ProxyMed, the holders of our Common Stock are entitled to receive pro rata the assets of ProxyMed which are legally available for distribution to shareholders. On August 17, 2001, we announced a 1-for-15 reverse stock split of our Common Stock whereby each 15 shares of Common Stock were exchanged for one new share of Common Stock. The holders of outstanding shares of Common Stock are entitled to receive dividends out of assets legally available for them at such times and in such amounts as the board of directors may from time to time determine. We have not paid any dividends and do not expect to pay cash dividends on our common stock in the foreseeable future.

Preferred Stock

In addition to series A, B and C Preferred Stock, our board of directors has the authority to issue 1,555,000 additional shares of Preferred Stock in one or more series and to fix the designation, relative powers, preferences and rights and qualifications, limitations or restrictions of all shares of each such series, including dividend rates, conversion rights, voting rights, redemption and sinking fund provisions, liquidation preferences and the number of shares constituting each such series, without any further vote or action by the shareholders. The issuance of Preferred Stock could decrease the amount of earnings and assets available for distribution to holders of our Common Stock or adversely affect the rights and powers, including voting rights, of the holders of Common Stock and could have the effect of delaying, deferring or preventing a change in control of ProxyMed without further action by the shareholders.

Series C Preferred Stock

Pursuant to the terms of a Subscription Agreement dated June 15, 2000, we sold, in a private placement to institutional and individual investors a total of $24,310,000 of 7% convertible senior secured notes due January 1, 2001. Together with the notes, we issued five-year warrants for the purchase of an aggregate of 810,333 shares of Common Stock at an exercise price of $15.00 per share. All of the Notes and warrants have been converted into shares of Series C Preferred Stock. The conversion price of the Series C Preferred Stock, the warrant exercise price, and number of shares of Common Stock issuable upon exercise of the warrants were subject to adjustment upon the occurrence of certain dilution events including, without limitation, certain issuances of Common Stock, Stock options or convertible securities issued after June 2001, or certain corporate transactions such as stock splits, mergers or asset sales. Certain of the foregoing adjustments, however, are no longer applicable. Shares of Series C Preferred Stock are immediately convertible into our Common Stock at any time by the holder at an initial conversion price of $15.00 per share. Shares of Series C Preferred Stock are subject to mandatory conversion if we raise more than $30 million in gross proceeds from the issuance of securities in a private or public placement or if the closing stock price of our Common Stock is trading at $45.00 for 20 consecutive trading days. If declared by our

Table of Contents

board of directors in its sole discretion, the Series C Preferred Stock is entitled to receive a 7% annual non-cumulative dividend, payable quarterly in cash or shares of Common Stock at our option. If paid in Common Stock, the Common Stock is valued at $15.00 per share, subject to adjustment. Dividends on Series C Preferred Stock are non-cumulative. Holders of more than two thirds of the outstanding Series C Preferred Stock have voted to amend the articles of designation governing the Series C Preferred Stock and the subscription agreement dated as of June 15, 2000. These amendments eliminate certain rights of the Series C Preferred shareholders, including anti-dilution provisions, voting rights and certain restrictive covenants agreed to by us. In the event of liquidation of the Company, the holders of the Series C Preferred Stock will continue to be entitled to a liquidation preference before any amounts are paid to the holders of Common Stock or any other security junior to Series C Preferred Stock. The liquidation preference is equal to an amount originally paid for the Series C Preferred Stock ($100 per share) plus accrued and unpaid dividends on any outstanding Series C Preferred Stock through the date of determination, if previously declared by our board of directors in its sole discretion. The holders of Series C Preferred Stock are entitled to one vote per share of Common Stock issuable upon the conversion of the Series C Preferred Stock and, except as otherwise provided by law, will vote as a single class with the holders of Common Stock on all matters submitted to a vote.

Certain Anti-Takeover Provisions

The Florida Business Corporation Act prohibits the voting of shares in a publicly-held Florida corporation that are acquired in a control share acquisition unless the holders of a majority of the corporation s voting shares (exclusive of shares held by officers of the corporation, inside directors or the acquiring party) approve the granting of voting rights as to the shares acquired in the control share acquisition or unless the acquisition is approved by the corporation s board of directors. A control share acquisition is defined as an acquisition that immediately thereafter entitles the acquiring party to vote in the election of directors within each of the following ranges of voting power: (i) one-fifth or more but less than one-third of such voting power; (ii) one-third or more but less than a majority of such voting power; and (iii) more than a majority of such voting power. The Florida Business Corporation Act also contains an affiliated transaction provision that prohibits a publicly-held Florida corporation from engaging in a broad range of business combinations or other extraordinary corporate transactions with an interested shareholder unless (i) the transaction is approved by a majority of disinterested directors before the person becomes an interested shareholder; (ii) the interested shareholder has owned at least 80% of the corporation s outstanding voting shares for at least five years; or (iii) the transaction is approved by the holders of two-thirds of the corporation s voting shares other than those owned by the interested shareholder. An interested shareholder is defined as a person who together with affiliates and associates beneficially owns more than 10% of the corporation s outstanding voting shares.

We are not subject to the Florida anti-takeover provisions under the Florida Business Corporation Act because we have elected to opt out of those provisions in our articles of incorporation or bylaws as permitted by the Florida law.

Transfer Agent and Registrar

Registrar and Transfer Company serves as transfer agent and registrar for our Common Stock. Its telephone number is (800) 525-7686.

Indemnification of Officers and Directors

Florida law provides that a corporation may indemnify any officer or director who is made a party to any third party suit or proceeding on account of being a director, officer or employee of the corporation against expenses, including attorney s fees, judgments, fines and amounts paid in settlement reasonably incurred by him in connection with the action, through, among other things, a majority vote of a quorum consisting of directors who were not parties to the suit or proceeding, if the officer or director: (1) acted in good faith and in a manner he reasonably believed to be in, or not opposed to, the best interests of the corporation; and (2) in a criminal proceeding, had no reasonable cause to believe his conduct was unlawful.

Our amended and restated articles of incorporation and bylaws provide for the indemnification of the officers and directors of the company for their actions and omissions up to the maximum extent permitted by law.

Table of Contents

The board of directors shall have the sole and exclusive discretion, on such terms and conditions as it shall determine, to indemnify, or advance expenses to, any person made, or threatened to be made, a party to any action, suit, or proceeding by reason of the fact that he is or was an officer, employee or agent of us, or is or was serving at our request as an officer, employee or agent of another corporation, partnership, joint venture, trust or other enterprise.

Table of Contents

PLAN OF DISTRIBUTION

The Selling Shareholders, which as used herein include donees, pledgees, transferees or other successors-in-interest selling shares of our Common Stock received after the date of this prospectus from a Selling Shareholder as a gift, pledge, partnership distribution or other transfer, may, from time to time, sell, transfer or otherwise dispose of any or all of their shares of Common Stock or interests in shares of Common Stock on any stock exchange, market or trading facility on which the shares are traded or in private transactions. These dispositions may be at fixed prices, at prevailing market prices at the time of sale, at prices related to the prevailing market price, at varying prices determined at the time of sale, or at negotiated prices.

The Selling Shareholders may use any one or more of the following methods when disposing of shares or interests therein:

on the Nasdaq Stock Market (or any other exchange on which the shares may be listed);

ordinary brokerage transactions and transactions in which the broker-dealer solicits purchasers;

block trades in which the broker-dealer will attempt to sell the shares as agent, but may position and resell a portion of the block as principal to facilitate the transaction;

purchases by a broker-dealer as principal and resale by the broker-dealer for its account;

an exchange distribution in accordance with the rules of the applicable exchange;

privately negotiated transactions;

short sales;

through the writing or settlement of options or other hedging transactions, whether through an options exchange or otherwise;

broker-dealers may agree with the Selling Shareholders to sell a specified number of such shares at a stipulated price per share;

a combination of any such methods of sale; and

any other method permitted pursuant to applicable law.

The Selling Shareholders may, from time to time, pledge or grant a security interest in some or all of the shares of Common Stock owned by them and, if they default in the performance of their secured obligations, the pledgees or secured parties may offer and sell the shares of common stock, from time to time, under this prospectus, or under an amendment to this prospectus under Rule 424(b) or under any applicable provision of the Securities Act amending the list of Selling Shareholders to include the pledgee, transferee or other successors in interest as Selling Shareholders under this prospectus. The Selling Shareholders also may transfer the shares of our Common Stock in other circumstances, in which case the transferees, pledgees or other successors in interest will be the selling beneficial owners for purposes of this prospectus. To the extent required, this prospectus may be amended or supplemented from time to time to describe a specific plan of distribution.

In connection with the sale of our Common Stock or interests therein, the Selling Shareholders may enter into hedging transactions with broker-dealers or other financial institutions, which may, in turn, engage in short sales of the Common Stock in the course of hedging the positions they assume. The Selling Shareholders may also sell shares of our common stock short and deliver these securities to close out their short positions, or loan or pledge the common stock to broker-dealers that in turn may sell these securities. The Selling Shareholders may also enter into option or other transactions with broker-dealers or other financial institutions or the creation of one or more derivative securities

which require the delivery to such broker-dealer or other financial institution of shares offered

Table of Contents

by this prospectus, which shares such broker-dealer or other financial institution may resell pursuant to this prospectus (as supplemented or amended to reflect such transaction).

The aggregate proceeds to the Selling Shareholders from the sale of our Common Stock offered by them will be the purchase price of our Common Stock less discounts or commissions, if any. Each of the Selling Shareholders reserves the right to accept and, together with their agents from time to time, to reject, in whole or in part, any proposed purchase of our Common Stock to be made directly or through agents. We will not receive any of the proceeds.

The Selling Shareholders also may resell all or a portion of the shares in open market transactions in reliance upon Rule 144 under the Securities Act, provided that they meet the criteria and conform to the requirements of that rule.

The Selling Shareholders and any underwriters, broker-dealers or agents that participate in the sale of the common stock or interests therein may be underwriters within the meaning of Section 2(11) of the Securities Act. Any discounts, commissions, concessions or profit they earn on any resale of the shares may be underwriting discounts and commissions under the Securities Act. Selling Shareholders who are underwriters within the meaning of Section 2(11) of the Securities Act will be subject to the prospectus delivery requirements of the Securities Act. The Selling Shareholders may indemnify any broker-dealer that participates in transactions involving the sale of the shares against certain liabilities, including liabilities arising under the Securities Act.

We have borne and will bear substantially all of the costs, expenses and fees in connection with the registration of the shares, other than any commissions, discounts or other fees payable to broker-dealers in connection with any sale of shares, which will be borne by the Selling Shareholder selling such shares of our Common Stock. We have agreed to indemnify the Selling Shareholders against certain liabilities, including liabilities under the Securities Act and state securities laws, relating to the registration of the shares offered by this prospectus.

In order to comply with the securities laws of some states, if applicable, the Common Stock may be sold in these jurisdictions only through registered or licensed brokers or dealers. In addition, in some states the Common Stock may not be sold unless it has been registered or qualified for sale or unless an exemption from registration or qualification requirements is available and is complied with.

The Selling Shareholders may be subject to the anti-manipulation rules of Regulation M, which may limit the timing of purchases and sales of shares of our Common Stock by such Selling Shareholders.

We will make copies of this prospectus (as it may be supplemented or amended from time to time) available to the Selling Shareholders for the purpose of satisfying the prospectus delivery requirements of the Securities Act.

We have agreed with the Selling Shareholders to keep the registration statement, of which this prospectus constitutes a part, continuously effective under the Securities Act until the earlier of (1) the date on which all shares covered by this prospectus may be sold immediately without registration under the Securities Act and without volume restrictions pursuant to Rule 144(k), and (2) such time as all of such Selling Shareholder s shares covered by this prospectus have been sold.

LEGAL MATTERS

The validity of the shares of Common Stock offered hereby has been passed upon for us by Holland & Knight LLP, Miami, Florida.

Table of Contents

EXPERTS

The consolidated financial statements of ProxyMed, Inc. and subsidiaries (the Company) as of December 31, 2004 and for the year ended December 31, 2004, and management s report on the effectiveness of internal control over financial reporting included in this Prospectus and the related financial schedule as of December 31, 2004 included elsewhere in the registration statement have been audited by Deloitte & Touche LLP, independent registered public accounting firm as stated in their reports appearing herein (which reports (1) express an unqualified opinion on the consolidated financial statements and financial statement schedule and include an explanatory paragraph regarding the Company s ability to continue as a going concern, (2) express an unqualified opinion on management s assessment regarding the effectiveness of internal control over financial reporting, and (3) express an unqualified opinion on the effectiveness of internal control over financial reporting) and have been so included in reliance upon the report of such firm given upon their authority as experts in accounting and auditing.

The financial statements of ProxyMed, Inc. and its subsidiaries as of December 31, 2003 and for each of the two years in the period ended December 31, 2003 included in this Prospectus and the related financial statement schedule for each of the two years in the period ended December 31, 2003 also included in this Prospectus have been so included in reliance on the report of PricewaterhouseCoopers LLP, an independent registered certified public accounting firm, given on the authority of said firm as experts in auditing and accounting.

The financial statements of PlanVista Corporation and its subsidiaries as of December 31, 2003 and for each of the three years in the period ended December 31, 2003 included in this Prospectus have been so included in reliance on the report of PricewaterhouseCoopers LLP, an independent registered certified public accounting firm, given on the authority of said firm as experts in auditing and accounting.

WHERE YOU CAN FIND ADDITIONAL INFORMATION

We have filed a registration statement on Form S-1 with the SEC for the stock offered pursuant to this prospectus. This prospectus does not include all of the information contained in the registration statement and its exhibits. We have included all material terms of the registration statement and the related exhibits and schedules that are referred to in this prospectus. You should refer to the registration statement and its exhibits for additional information. We are also required to file annual, quarterly and special reports, proxy statements and other information with the SEC.

You can read our SEC filings, including the registration statement, over the Internet at the SEC s web site at *http://www.sec.gov*. You may also read and copy any document we file with the SEC at its public reference facilities at 100 F Street, N.E., Room 1580, Washington, D.C. 20549. You may also obtain copies of the documents at prescribed rates by writing to the Public Reference Room of the SEC at 100 F Street, N.E., Room 1580, Washington, D.C. 20549. Please call the SEC at (202) 551-8090 for further information on the operation of the public reference facilities.

Table of Contents

PROXYMED, INC.
INDEX TO FINANCIAL STATEMENTS

Table of Contents

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Stockholders of
ProxyMed, Inc.
Atlanta, Georgia

We have audited the accompanying consolidated balance sheet of ProxyMed, Inc. and its subsidiaries (the Company) as of December 31, 2004, and the related consolidated statements of operations, stockholders equity, and cash flows for the year then ended. Our audit also included the financial statement schedule listed in the Index at Item 15(a)(2) for the year ended December 31, 2004. These financial statements and financial statement schedule are the responsibility of the Company s management. Our responsibility is to express an opinion on the financial statements and financial statement schedules based on our audit. The financial statements and financial statement schedule of the Company for the years ended December 31, 2003 and 2002 were audited by other auditors whose report, dated March 25, 2004, expressed an unqualified opinion on the financial statements and financial statement schedule and included an explanatory paragraph that described the adoption of Financial Accounting Standards Board Statement No. 142, *Goodwill and Other Intangible Assets* discussed in Note 9 to the financial statements.

We conducted our audit 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. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, such consolidated financial statements present fairly, in all material respects, the financial position of ProxyMed, Inc. and its subsidiaries as of December 31, 2004, and the results of their operations and their cash flows for the year then ended, in conformity with accounting principles generally accepted in the United States of America. Also, in our opinion, such financial statement schedule, when considered in relation to the basic consolidated financial statements taken as a whole, present fairly, in all material respects, the information set forth therein for the year ended December 31, 2004.

The accompanying consolidated financial statements for the year ended December 31, 2004 have been prepared assuming that the Company will continue as a going concern. As discussed in Note 21 to the financial statements, the Company s potential inability to pay certain current debt obligations when due raises substantial doubt about its ability to continue as a going concern. Management s plans concerning these matters are described in Note 12*(a)*. The financial statements do not include any adjustments that might result from the outcome of this uncertainty.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the effectiveness of the Company s internal control over financial reporting as of December 31, 2004, based on the criteria established in *Internal Control Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated March 16, 2005 expressed an unqualified opinion on management s assessment of the effectiveness of internal control over financial reporting and an unqualified opinion on the effectiveness of the Company s internal control over financial reporting.

/s/ Deloitte & Touche LLP
Atlanta, Georgia
March 16, 2005

Table of Contents

REPORT OF INDEPENDENT REGISTERED CERTIFIED PUBLIC ACCOUNTING FIRM

To the Board of Directors and the
Shareholders of ProxyMed, Inc.

In our opinion, the accompanying consolidated financial statements listed in the index appearing on page F-1 present fairly, in all material respects, the financial position of ProxyMed, Inc. and its subsidiaries (the Company) at December 31, 2003 and the results of their operations and their cash flows for each of the two years in the period ended December 31, 2003 in conformity with accounting principles generally accepted in the United States of America. In addition, in our opinion, the financial statement schedule for each of the two (2) years in the period ended December 31, 2003 listed in the accompanying index appearing on Page F-1 presents fairly, in all material respects, the information set forth therein when read in conjunction with the related consolidated financial statements. These financial statements and financial statement schedule are the responsibility of the Company s management; our responsibility is to express an opinion on these financial statements and financial statement schedule based on our audits. We conducted our audits of these statements 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. An audit 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, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

/s/ PricewaterhouseCoopers LLP
Fort Lauderdale, Florida
March 25, 2004

Table of Contents

PROXYMED, INC. AND SUBSIDIARIES
Consolidated Balance Sheets
December 31, 2003 and 2004 and September 30, 2005 (unaudited)
(amounts in thousands except for share and per share data)

	2003	2004	2005 (unaudited)
Assets			
Current assets:			
Cash and cash equivalents	$ 5,333	$ 12,374	$ 6,756
Accounts receivable trade, net of allowance for doubtful accounts of $882, $3,168 and $4,306, respectively	10,434	17,591	16,335
Other receivables	187	312	110
Inventory, net	3,347	1,775	1,163
Other current assets	1,908	1,399	1,567
Total current assets	21,209	33,451	25,931
Property and equipment, net	4,772	4,801	4,303
Goodwill, net	30,775	93,604	26,444
Purchased technology, capitalized software and other intangible assets, net	15,884	52,305	18,746
Restricted cash	291	75	75
Other long-term assets	199	167	133
Total Assets	$ 73,130	$ 184,403	$ 75,632
Liabilities and Stockholders Equity			
Current liabilities:			
Notes payable and current portion of long-term debt	$ 1,712	$ 2,178	$ 637
Related party debt See Notes 12(a) and 21		18,394	
Accounts payable and accrued expenses and other current liabilities	8,264	13,637	13,770
Deferred revenue	721	691	419
Income taxes payable		215	1,037
Total current liabilities	10,697	35,115	15,863
Convertible notes	13,137	13,137	13,137
Other long-term debt	2,057	206	12,129
Long-term deferred revenue and other long-term liabilities	1,461	863	2,137
Total liabilities	27,352	49,321	43,266

Commitments and contingencies see Notes 18 and 19			
Stockholders equity:			
Series C 7% Convertible preferred stock $.01 par value Authorized 300,000 shares; issued 253,265 shares; outstanding 2,000; liquidation preference $200			
Common stock $.001 par value. Authorized 30,000,000 shares; issued and outstanding 6,784,118, 12,626,182 and 12,704,087 shares, respectively	7	13	13
Additional paid-in capital	146,230	239,255	239,927
Unearned compensation		(113)	(45)
Accumulated deficit	(100,273)	(104,073)	(207,529)
Note receivable from stockholder	(186)		
Total stockholders equity	45,778	135,082	32,366
Total liabilities and stockholders equity	$ 73,130	$ 184,403	$ 75,632

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

Table of Contents

PROXYMED, INC. AND SUBSIDIARIES
Consolidated Statements of Operations
Years Ended December 31, 2002, 2003 and 2004 and the Nine Months Ended September 30, 2004 (unaudited) and 2005 (unaudited)
(amounts in thousands except for share and per share data)

	2002	2003	2004	Nine Months Ended September 30, 2004 (unaudited)	Nine Months Ended September 30, 2005 (unaudited)
Net Revenues					
Transaction fees, cost containment services and license fees	$ 28,455	$ 51,813	$ 73,538	$ 55,807	$ 52,699
Communication devices and other tangible goods	21,727	19,743	16,708	11,858	7,565
	50,182	71,556	90,246	67,665	60,264
Costs and expenses:					
Cost of transaction fees, cost containment services and license fees excluding depreciation and amortization	8,858	15,917	22,626	16,041	17,867
Cost of laboratory communication devices and other tangible goods excluding depreciation and amortization	17,158	16,504	11,586	9,856	3,013
Selling, general and administrative expenses	20,152	35,809	48,023	35,438	37,122
Depreciation and amortization	2,636	6,316	9,763	7,086	7,687
Loss on disposal of assets		111	47		
Litigation settlement			175		
Write-off of impaired and obsolete assets	38	541			96,416
	48,842	75,198	92,220	68,421	162,105
Operating income (loss)	1,340	(3,642)	(1,974)	(756)	(101,841)
Other income (expense), net	265	(496)	134	133	(175)
Interest income (expense), net	345	(862)	(1,920)	(1,379)	(1,440)