COMPUTERIZED THERMAL IMAGING INC
Form 10QSB
May 15, 2006

U.S. SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-QSB

(Mark One)

[X] QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended March 31, 2006

[ ] 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: 001-16253

COMPUTERIZED THERMAL IMAGING, INC.
(Exact name of Registrant as specified in its charter)

NEVADA	87-0458721
(State or other jurisdiction of incorporation or organization)	(IRS Employer Identification No.)
1719 West 2800 South Ogden, Utah	84401
(Address of principal executive offices)	(Zip Code)

(801) 776-4700
(Registrant's telephone number, including area code)

Check whether the issuer (1) filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act during the past 12 months (or for such shorter period that the registrant was required to file such reports) and (2) has been subject to such filing requirements for the past 90 days. Yes[X] No[ ]

State the number of shares outstanding of each of the issuer's classes of common equity, as of the latest practicable date: Common stock, par value $0.001, of which 114,561,698 shares were issued and outstanding as of April 30, 2006.

Transitional Small Business Disclosure Format (check one): Yes [ ] No [X]

COMPUTERIZED THERMAL IMAGING, INC.

FORM 10-QSB

QUARTERLY REPORT

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PART I - FINANCIAL INFORMATION
ITEM 1. UNAUDITED FINANCIAL STATEMENTS

COMPUTERIZED THERMAL IMAGING, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS

	MARCH 31, 2006	JUNE 30, 2005
ASSETS	(unaudited)	
CURRENT ASSETS:		
Cash and cash equivalents	$ 23,288	$ 51,728
Inventories	58,022	87,276
Prepaid expenses	33,809	33,809
Total Current Assets	115,119	172,813

Property, Equipment & Software	1,004,560	1,006,504
Accumulated Depreciation	(999,310)	(998,979)
NET PROPERTY PLANT & EQUIPMENT (Net)	5,250	7,525
INTANGIBLE ASSETS:		
Intellectual Property Rights, less accumulated amortization of $22,109 and $20,107 respectfully	10,738	12,740
TOTAL ASSETS	$ 131,107	$ 193,078
LIABILITIES & STOCKHOLDERS' EQUITY (DEFICIT)		
CURRENT LIABILITIES:		
Accounts Payable	$ 243,559	$ 558,045
Accrued Employee Costs	281,467	229,498
Other Accrued Liabilities	304,000	325,764
Short-term Note Payable with Interest	699,677	333,891
Deferred Revenue	1,239	669,991
Total Current Liabilities	1,529,942	2,117,189
LONG-TERM NOTE PAYABLE	117,936	114,181
TOTAL LIABILITIES	1,647,878	2,231,370
STOCKHOLDERS' EQUITY (DEFICIT)		
Convertible Preferred Stock, no par value, 3,000,000 shares authorized; none issued	--	--
Common Stock, $.001 par value, 200,000,000 shares authorized, 114,561,698 and 114,561,698 issued and outstanding on March 31, 2006 and June 30, 2005, respectively	114,561	114,561
Additional Paid-in Capital	95,462,475	95,462,475
Deficit Accumulated	(97,093,807)	(97,615,328)
TOTAL STOCKHOLDERS' EQUITY (DEFICIT)	(1,516,771)	(2,038,292)
TOTAL LIABILITIES & STOCKHOLDERS' EQUITY (DEFICIT)	$ 131,107	$ 193,078

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

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COMPUTERIZED THERMAL IMAGING, INC.
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(Unaudited)

	FOR THE THREE MONTHS ENDED MARCH 31,		F NINE MO MA
	2006	2005	2006
REVENUE			

PS	5,813	47,425	38,29
TIP	2,488	--	20,50
Turbine	--	--	-
Other Services - Nanda	660,495	28,325	660,49
Freight	270	--	1,02
NET REVENUE	669,066	75,750	720,31
COST OF SALES			
Materials	1,507	23,211	10,04
Impairments	--	--	24,48
Freight	1,753	--	10,73
TOTAL COST OF SALES	3,260	23,211	45,25
GROSS MARGIN (DEFICIT)	665,806	52,539	675,05
OPERATING EXPENSES			
General & Administration	161,906	23,450	478,86
Depreciation & Amortization	2,413	10,584	4,27
Litigation Settlement	--	--	1,00
Marketing	--	(1,685)	-
R & D	--	17,118	-
TOTAL OPERATING EXPENSES	164,319	49,467	484,14
OPERATING INCOME (LOSS)	501,487	3,072	190,91
OTHER INCOME / EXPENSE			
Interest Income	308	4	2,46
Interest Expense	(10,820)	(4,535)	(30,734
Other	1	7	(69
Gain from Extinguishment of Debt	358,945	--	358,94
TOTAL OTHER INCOME / EXPENSE	348,434	(4,524)	330,61
NET INCOME (LOSS)	$ 849,921	$ (1,452)	521,52
WEIGHTED AVERAGE SHARES OUTSTANDING	114,561,698	114,561,698	114,561,69
BASIC AND DILUTED INCOME (LOSS) PER COMMON SHARE	$ 0.01	$ (0.00)	$ 0.0

The accompanying notes are an integral part of these consolidated financial statem

COMPUTERIZED THERMAL IMAGING, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

	For the Nine Months Ended March 31,	
	2006	2005

CASH FLOWS FROM OPERATING ACTIVITIES:		
Net Income (Loss)	$ 521,521	$(288,146)
Depreciation and Amortization	4,277	27,683
Gain on Extinguishment of Debt	(358,945)	--
Interest Expense on Convertible Debenture	--	26,447
Changes in Operating Assets and Liabilities:	--	1,391
Accounts Receivable - Trade	--	26,447
Accounts Receivable - Other	--	1,391
Inventories	29,254	40,295
Prepaid Expenses	--	47,665
Accounts Payable	177,860	37,038
Accrued Liabilities	(58,655)	(25,337)
Deferred Revenues	(668,752)	(29,608)
Net Cash Used in Operating Activities	(353,440)	(162,572)
CASH FLOWS FROM INVESTING ACTIVITIES:		
Net Cash Provided by (Used in) Investing Activities	--	--
CASH FLOWS FROM FINANCING ACTIVITIES:		
Proceeds from Loan	325,000	--
Net Cash Provided by Financing Activities	325,000	--
NET INCREASE (DECREASE) IN CASH	(28,440)	(162,572)
CASH AT BEGINNING OF PERIOD	51,728	168,955
CASH AT END OF PERIOD	$ 23,288	$ 6,383

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

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COMPUTERIZED THERMAL IMAGING, INC.
Notes to Condensed Consolidated Financial Statements
March 31, 2006
(UNAUDITED)

NOTE A. UNAUDITED FINANCIAL STATEMENTS AND BASIS OF PRESENTATION

The condensed consolidated financial statements of Computerized Thermal Imaging (the "Company") for the three and nine-month periods ended March 31, 2006 and 2005 are unaudited. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation of the Company's results of operation for the periods presented have been included. These interim statements should be read in conjunction with the audited consolidated financial statements and footnotes thereto contained in

the Company's most recent Annual Report on Form 10-KSB for the Year Ended June 30, 2005. The consolidated results of operations for the three and nine-month periods ended March 31, 2006 are not necessarily indicative of the results to be expected for the full year.

Certain amounts from the prior period financial statements have been reclassified to conform to current period presentation.

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions, including, for example, accounts receivable allowances, inventory obsolescence reserves, deferred tax valuation allowances, and reserves for pending or threatened litigation. These assumptions affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from these estimates.

The accompanying condensed consolidated financial statements have been prepared assuming the Company will continue as a going concern. In its Annual Report on Form 10-KSB for the Year Ended June 30, 2005, the Company reported that its recurring losses from operations, negative cash flows from operations, need for additional working capital and continuing struggle to obtain FDA approval for its primary product raised substantial doubt about the Company's ability to continue as a going concern. The Company's independent auditors have also expressed their doubts about the Company's ability to continue as a going concern and have accordingly qualified their report on the Company's financial statements for the year ended June 30, 2005.

In order to pursue its existing plan of operations, the Company will have to secure additional financing through the sale of equity, the incurrence of debt or the sale of assets, including the Company's intellectual property, or some other method. There can be no assurance that capital will be available from any source or, if available, that the terms and conditions associated with such capital will be acceptable to the Company. If the Company raises equity or debt capital, the sale of these securities could dilute existing shareholders, and borrowings from third parties could result in assets being pledged as collateral and could provide loan terms that could adversely affect the Company's operations and the price of its capital stock.

The accompanying condensed consolidated financial statements do not include any adjustments relating to the recoverability and classification of recorded asset amounts or the amounts and classification of liabilities that might be necessary if the Company is unable to continue as a going concern.

NOTE B. REVENUE RECOGNITION

The Company generates revenues from sales of its products and from services provided to its customers. The Company sells its products to independent distributors and to end customers. With the exception of sales transactions in which a customer may return a defective product, the Company does not provide its customers with other rights to return products.

The Company recognizes revenue from its product sales to end customers upon shipment of products when persuasive evidence of an agreement exists,

delivery of the product has occurred, no significant Company obligations remain, the fee is fixed or determinable, and collectibility is probable. If these conditions are not met, revenue is deferred until such obligations and conditions are fulfilled. If the Company retains an ongoing obligation under a sales arrangement, revenue is deferred until all of the Company's obligations are fulfilled.

The Company has adopted the practice of deferring revenue on shipments to distributors until cash payment from the distributor is received by the Company, which is generally when the product is sold by the distributor to the end customer.

Certain of the Company's products contain software that is not considered incidental to the product. Sales of those products are subject to the provisions of AICPA Statement of Position No. 97-2, SOFTWARE REVENUE RECOGNITION, as amended, which requires the deferral of revenue from certain multiple-element arrangements. The Company defers revenue from multiple-element arrangements until all elements have been delivered.

Service revenue is derived from service of equipment previously sold but not covered by warranty. Service revenue is recognized upon the completion of the services provided. The Company offers extended warranties on certain of its products. Warranty revenue is recognized ratably over the period of the agreement as services are provided.

NOTE C. DEFERRED REVENUE

Deferred revenues at March 31, 2006 consisted of deferred warranty revenues.

DEFERRED REVENUES

	31-MAR 2006	31-DEC 2005	30-SEP 2005	30-JUN 2005
NANDA LICENSING	-	660,000	660,000	660,000
WARRANTY REVENUE	1,239	3,727	6,859	9,991
TOTAL DEFERRED REVENUE	$ 1,239	$663,727	$666,859	$669,991

The Company's Manufacturing License Agreement (the "NanDa Agreement") with NanDa, Thermal Medical Technology, Inc. ("NanDa") was billed in stages. The Company billed NanDa $660 thousand to date and received payment of $660 thousand. The NanDa Agreement obligates the Company to provide training services for NanDa employees in the United States. The Company has provided the training services for NanDa employees in the United States and according to the Company's revenue recognition policy the deferred revenue has been recognized. The Company believes NanDa's failure to perform certain material obligations required pursuant to the terms of the NanDa Agreement constitutes a valid basis for termination of the NanDa Agreement. Accordingly, the Company intends to give notice of termination to NanDa.

NOTE D. INVENTORIES

Inventories are stated at the lower-of-cost or market with cost determined using the first-in first-out method of accounting. As of the dates set forth below, the Company's inventories consisted of the following:

INVENTORY

	MARCH 1, 2006	JUNE 30, 2005
Raw Materials	$ 537,708	$ 536,053
Finished Goods	181,980	190,887
Inventory Reserve	(661,666)	(639,664)
TOTAL	58,022	87,276

Inventory at March 31, 2006 consisted of approximately $182 thousand of finished goods ready for sale and $538 thousand of raw materials. The Company has impaired its inventory by 92% or $662 thousand due to concerns regarding the Company's ability to continue as a going concern. The impairment is held in a reserve account.

The Company has in the past reserved for excess and obsolete inventory by comparing inventory on hand to estimated consumption during the next twelve months. Consumption is estimated by annualizing trailing three or six -month sales volumes, adjusting those volumes for known activities and trends, then comparing forecast consumption to quantity on hand. However, the Company evaluates all inventories to determine if the total impaired book value could be recovered if liquidation becomes necessary. The Company impaired the BCS inventory in the amount of $24 thousand for the nine-months ended March 31, 2006.

NOTE E. INCOME TAXES

The Company accounts for income taxes using the liability method. Under this method, the Company records deferred income taxes to reflect future year tax consequences of temporary differences between the tax basis of assets and liabilities and their financial statement amounts. The Company has reviewed its net deferred tax assets, together with net operating loss carry-forwards, and

has provided a valuation allowance to reduce its net deferred tax assets to their net realizable value. Due to the uncertainty regarding the Company's volatility to continue as a going concern, there are no deferred tax assets.

NOTE F. CONTINGENCIES

SEC INVESTIGATION

In December 2002, the Company was requested to provide certain documents to the Securities and Exchange Commission (the "Commission") and the U.S. Department of Justice in connection with an investigation regarding possible violations of the insider trading prohibitions found in the federal securities laws. The Company has responded to the Commission's requests for copies of documentation, and members of the Company's management have provided

testimony to the Commission. To date, the Company has incurred approximately $650,000 in legal costs in complying with these requests. The Company also may be required to indemnify its officers and directors in connection with fees incurred in connection with these investigations. The Company's efforts to respond to the Commission's requests have required, and in the future may require, significant additional legal expenses, may make fund raising more difficult if not impossible, and will divert attention away from the Company's day-to-day operations.

INDEMNIFICATION

Under the Company's bylaws and contractual agreements, the Company may be required to indemnify its current and former officers and directors who are parties to litigation or other proceedings by providing legal defense through the Company's attorneys (or reimbursing the parties for their own attorneys) and covering all damages the parties may suffer if the plaintiffs are successful.

OTHER LEGAL PROCEEDINGS

The Company is involved in certain other litigation matters in the normal course of business which management currently believes are not likely to result in any material adverse effects on the Company's financial position, results of operations, or net cash flows.

NOTE G. RECENT DEVELOPMENTS

Since January 2006, the Company has been engaged in implementing its re-directed business strategy, which is focused on strengthening new sales of the Company's products and aftermarket product support pipelines.

On March 6, 2006 the Company announced the execution of sales and lease agreements for placement of the Company's medical equipment. One of the Company's Thermal Imaging Processor ("TIP") suites was placed at Tampa Bay Orthopaedic Specialists in Tampa Florida ("TBOS"). TBOS is one of the largest orthopaedic groups in central Florida and is a leading orthopaedic surgical and physical therapy facility specializing in surgical treatment of hands, upper extremities, feet and ankles, as well as treatment of repetitive use injuries.

On March 28, 2006 the Company announced the placement of thermal imaging medical equipment at the University of New England's Biomechanics Research Laboratory in Portland, Maine. The system will be implemented as a key component used for studies on peripheral nerve injuries.

During March of 2006, the Company also contracted with Covina Wellness Center in Covina, CA to sell one TIP and two Photonic Stimulators. The Covina Wellness Center specializes in physical therapy and women's health. The center's management has indicated that TIP screening for breast cancer will be one of the new services offered in the clinic.

On June 30, 2004 the Company filed a "Citizen Petition" with the FDA contending that consideration of the Company's application for pre-market approval was severely and improperly prejudiced because of pervasive bias against the Company by the FDA staff reviewers who improperly undermined the review of the Company's application and ultimately caused the FDA to reject that application. The Company is seeking internal documents within the FDA to

determine the basis for the FDA staff's behavior.

NOTE H. STOCK WARRANTS AND OPTIONS

A summary of warrant and stock option activity for the period from July 1, 2005, through March 31, 2006 is as follows:

	2005		2004	
	Shares	Weighted Average Exercise Price	Shares	Weighted Average Exercise Price
Outstanding June 30	4,384,958	1.26	3,592,023	1.27
Granted	--	--	175,000	0.10
Exercised	--	--	--	--
Forfeited	(926,026)	--	(77,780)	1.01
Outstanding at end of year	3,458,932	1.26	3,689,243	1.37
Exercisable at March 31, 2006	3,458,932	1.26	3,689,243	1.37

Periodically, the Company has issued incentive stock options to employees and officers and non-qualified options to directors and outside consultants to promote the success of the Company and enhance its ability to attract and retain the services of qualified persons.

The Company has 3,458,932 options outstanding and issued under its 1997 Stock Option and Restricted Stock Plan (the "Plan") since its adoption, and could issue an additional aggregate of 6,541,068 options and shares. The Plan permits restricted stock grants to employees, officers, directors and consultants at prices that may be less than 100% of the fair market value of the Company's common stock on the date of issuance. The Company also has outstanding 150,000 non-statutory stock options issued outside the Plan. Options issued under the Plan will have variable terms based on the services provided and will generally vest on the date of grant.

Modifications to the terms of previously fixed stock options or awards granted to Company employees are accounted for in accordance with APB Opinion No. 25 and Interpretation No. 44, ACCOUNTING FOR CERTAIN TRANSACTIONS INVOLVING

STOCK COMPENSATION--AN INTERPRETATION OF ACCOUNTING PRINCIPLES BOARD (APB) OPINION NO. 25 ("FIN 44"). During the year ended June 30, 2005 the Company did not re-price any options. As a result of the Company's significant reduction in personnel during the year ended June 30, 2005, nearly all those employees holding options that had been re-priced in prior years are no longer employed by the Company and their rights to exercise their options have lapsed.

If compensation cost for options or awards granted to employees had been determined based on SFAS No. 123, the Company's net loss and basic and diluted loss per common share would have not changed materially.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OR PLAN OF OPERATION

Forward-Looking Statements Concerning the Company's Business

The statements contained in this Quarterly Report on Form 10-QSB that are not purely historical are "forward-looking statements" within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. All forward-looking statements involve various risks and uncertainties. Forward-looking statements contained in this report include statements regarding the Company's business plans, market opportunities and acceptance, expectations, goals, revenues, financial performance, strategies, mission and intentions for the future. Such forward-looking statements are included under this "Management's Discussion and Analysis or Plan of Operation" and encompass the Company's beliefs, expectations, hopes or intentions regarding future events. Words such as "expects," "believes," "anticipates," "intends," "plans," "seeks," "may," "should," "likely," and similar expressions also identify forward-looking statements. All forward-looking statements included in this report are made as of the date hereof, based on information available to the Company as of such date, and the Company assumes no obligation to update any forward-looking statement. It is important to note that such statements may not prove to be accurate and that our actual results and future events could differ materially from those anticipated in such statements. Among the factors that could cause actual results to differ materially from our expectations are those described under "--Factors that May Affect Future Results." All subsequent written and oral forward-looking statements attributable the Company or persons acting on its behalf are expressly qualified in their entirety by this section and other factors included elsewhere in this report.

Overview

The Company's mission is to improve the quality of life through the development and deployment of thermal imaging and associated technologies. While the Company's infrared technology has a vast array of existing and potential applications, its primary focus is in medical and industrial application. The Company markets two FDA-cleared pain management products, a diagnostic Thermal Imaging Processor (camera) and an infrared light therapy device called the Photonic Stimulator. The Company designs, manufactures and markets thermal imaging devices and services used for clinical diagnosis and pain management.

The Company's current products are the Photonic Stimulator and the Thermal Image Processor ("TIP"). The Company has historically marketed its products with an internal sales force and through independent distributors. At present, however, due to the Company's troubled financial condition, the Company is not actively marketing its products with the exception of the Company's web page (www.cti-net.com). To date, the Company's revenues have been generated principally from sales of the Photonic Stimulator, TIP, and services provided in connection with the Company's medical and industrial products.

Given the Company's inability to market its principal product unless the Company secures FDA pre-market approval, the Company's needs to raise capital to fund its operations, the Company's history of losses ($97.1 million since inception), and the risk of pending or future litigation, the Company's independent auditor's opinion dated May 2006 contains a "going concern qualification," meaning that the Company's independent auditors have indicated

that there is substantial doubt as to the Company's ability to continue as a going concern. The Company's efforts to raise additional funds to date have been only marginally successful. Since the FDA's rejection of the Company's application for pre-market approval of the BCS 2100 in December 2002, the Company has raised approximately $500 thousand in advances under an equity line of credit with Beach Boulevard, $1.32 million through a private issuance of restricted stock, $660 thousand from its Manufacturing License Agreement (the "NanDa Agreement") with NanDa Thermal Medical Technology, Inc. ("NanDa") and $645 thousand from short-term notes. The Company has pursued additional financing transactions, but, as of the date of this Report, the Company has been unsuccessful in its efforts to raise additional capital. Regardless of the FDA's ultimate decision regarding the Company's application for pre-market approval of the Company's Breast Cancer System 2100 (the "BCS2100"), the Company will require additional capital to execute the Company's operating plan, which may include more clinical trials, research and development and marketing and manufacturing expenses.

The following discussion and analysis of the Company's consolidated financial condition and results of operations should be read in conjunction with the Company's audited condensed consolidated financial statements and notes thereto contained in the Company's Annual Report on Form 10-KSB for the fiscal year ended June 30, 2005.

CRITICAL ACCOUNTING POLICIES

The preparation of financial statements requires the Company to estimate the effect of various matters that are inherently uncertain as of the date of the financial statements. Each of these required estimates varies in regard to the level of judgment involved and its potential impact on the Company's reported financial results. Estimates are deemed critical when a different estimate could have reasonably been used or where changes in the estimate are reasonably likely to occur from period to period, and would materially impact the Company's financial condition or results of operations. The Company's significant accounting policies are discussed in Note A of the Notes to Condensed Consolidated Financial Statements. Critical estimates inherent in these accounting policies are discussed in the following paragraphs. The Company's management has discussed the development and selection of these critical accounting policies with the Audit Committee of the Company's Board of Directors.

CASH AND CASH EQUIVALENTS -- Cash and cash equivalents include cash in checking accounts and short-term highly liquid investments with an original maturity of one year or less.

REVENUE RECOGNITION --Revenue recognition is a significant business process that requires management to make estimates and assumptions. The Company recognizes revenue from product sales after shipment when persuasive evidence of an agreement exists, delivery of the product has occurred, no significant obligations remain, the price or fee is fixed or determinable, and collection is probable. If these conditions are not met, revenue is deferred until such obligations and conditions are fulfilled.

The Company's standard domestic terms for its medical products sold to end-user customers are "prepaid," and the Company's standard international terms for the Company's medical products require payment in cash or placement of a

letter of credit before shipment. On occasion, the Company offers extended payment terms beyond its normal business practices, usually in connection with providing an initial order of demonstration equipment to a new domestic distributor. The Company considers fees on these extended terms agreements not fixed and collectibility less than probable and defers the revenue until receipt of payment. The Company sells separate extended warranty contracts for the Company's TIP and Photonic Stimulator and recognizes revenue from those arrangements ratably over the contract life. The Company does not offer rights or return privileges in sales agreements.

RESEARCH AND DEVELOPMENT EXPENSES -- The Company expenses as incurred the direct, indirect and purchased research and development costs associated with the Company's products. The Company believes this method is conservative given the product and market acceptance risk inherent to the Company's products and reduces administrative burden and cost.

IMPAIRMENT OF LONG-LIVED ASSETS -- The Company follows the provisions of Financial Accounting Standards Board ("FASB") SFAS No. 141, Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of, which requires that if the sum of the future cash flows expected to result from the assets, undiscounted and without interest charges, is less than a company's reported value of the assets, the asset is not recoverable and the company must recognize an impairment. The amount of impairment to be recognized is the excess of the reported value of the assets over the fair value of those assets and is recorded as impairment expense on the Company's statements of operations. In estimating impairments, management makes assumptions about future cash flows and fair value that are inherently uncertain, can significantly affect the results and may differ from actual future results.

INVENTORY RESERVES -- In the past, the Company reserved for excess and obsolete inventory by comparing inventory on hand to estimated consumption during the next twelve months. Consumption is estimated by annualizing trailing three or six month sales volumes, adjusting those volumes for known activities and trends, and then compare forecast consumption to quantity on hand. However, the Company evaluates all inventories to determine if the total impaired book value could be recovered if liquidation is necessary.

TRENDS/UNCERTAINTIES AFFECTING CONTINUING OPERATIONS

The Company is exposed to the opportunities and risks usually associated with marketing and manufacturing novel products, including staff retention and recruiting, market acceptance of the Company's products, product warranty, bad debts and inventory obsolescence. The Company expects to earn revenues from the sale of its products, but there is no guarantee that these revenues will recover all the costs of marketing, selling and manufacturing of the products.

The Company is conducting only Internet marketing efforts at present due to the Company's current lack of resources. If the Company is able to acquire additional capital, of which there can be no assurance, the Company hopes to be able to resume marketing efforts by building relationships with manufacturers, medical equipment dealers, physicians and clinical investigators; communicating with target markets by attending trade shows and conferences, making direct sales calls, and sponsoring clinics in which the Company could introduce and demonstrate its products. The Company believes marketing medical

products through trade shows, conference presentations, direct mail and inside sales, augmented with dealers, provides a low-cost, high-leverage approach to diagnostic imaging and pain management practitioners.

If resources permit, the Company hopes to be able to organize clinical studies with institutions and practitioners to obtain user feedback and to secure technical papers for training and marketing purposes. These strategies would represent a significant investment of time and resources and in the past have provided useful information; however, there can be no guarantee that these strategies will lead to market acceptance of the Company's products.

To date, the Company has had limited operating revenues from the sale of its products and services ($4 million in total revenues since inception). The Company cannot provide any assurance that it will achieve profitability in the future. The Company's immediate priority is to produce revenue by selling TIP and Photonic Stimulator inventory, then, to expand the Company's market in Canada where the Company has obtained the necessary licenses for current product offerings, to pursue the U.S. market for the Company's TIP and Photonic Stimulator; and to reconcile issues regarding the BCS2100 presented to the FDA in the Company's Citizens Petition. At this time, the Company is unsure how much time and additional financing will be required to resolve issues with the FDA. The Company can offer no assurance that the Company will ever be able to resolve the FDA issues. The Company is also unsure about the ability to raise additional financing which will be required to continue the Company's business operations. These uncertainties, among others, raise doubts about the Company's ability to continue as a going concern.

FACTORS THAT MAY AFFECT FUTURE RESULTS

The Company's operating results and financial condition are subject to substantial risks and uncertainties. You should consider carefully the following risk factors, in addition to other information contained in this Report as you evaluate the Company and its business. Any one or more of these factors could cause actual results of the Company's operations to differ materially from projected results.

- The Company and its independent public accountant have determined that unless the Company is able to raise additional capital, it will not likely continue as a going concern.

- The Company expects to continue to incur losses, deficits, and deficiencies in liquidity for the foreseeable future, unless the Company is able to finalize agreements for additional capital investments.

- A failure to raise additional capital could cause the Company to severely curtail operations, which would likely result in immediate and substantial dilution to the Company's shareholders, or cease operations entirely, which would likely eliminate any value in the Company's common stock.

- The volatility in the market price of the Company's common stock could continue, which would adversely affect shareholder value.

- The Company can issue preferred stock or sell other securities or

other financing instruments, including convertible debt, which would result in significant dilution to existing shareholders.

- If the Company is unsuccessful in preventing others from using its intellectual property, the Company could lose a competitive advantage. If the Company's intellectual property infringes the rights of other parties, the Company could incur damages or be forced to cease using, marketing or selling those products.

- The Company does not have product liability insurance; if the Company is made subject to a products liability claim, whether or not the claim is meritorious, the Company's results of operation and financial condition may be adversely affected.

The foregoing factors should be read in conjunction with the Company's audited condensed consolidated financial statements, notes thereto and risk factors set forth in the Company's Annual Report on Form 10-KSB for the fiscal year ended June 30, 2005 (the "Form 10-KSB"). Many of the risks identified above are discussed in greater detail in the Form 10-KSB.

RESULTS OF OPERATIONS

THREE AND NINE-MONTHS ENDED MARCH 31, 2006, COMPARED TO THE THREE AND NINE-MONTHS ENDED MARCH 31, 2005

REVENUES

Total revenues for the three months ended March 31, 2006 increased $593 thousand, from $76 thousand in March of 2005 to $669 thousand in March 2006. Revenues for the nine-months ending March 31, 2006 increased $512 thousand, from $208 thousand in March of 2005 to $720 thousand March of 2006. The Company's revenues reflect a 783% increase in three months and 245% increase in nine-months. In both the three and nine-month periods of 2006 the increase in revenues is primarily attributable to the recognition of deferred revenue from Nanda totaling $660 thousand.

Six thousand dollars of the Company's revenues resulted from product sales and $2 thousand from warranty revenue recognized in the period ending March 31, 2006. The same three-month period in 2005 produced product revenues of $47 thousand with service revenues of $28 thousand.

There were no unfilled orders as of March 31, 2006. The Company did not have any foreign sales in the past nine months ended March 31, 2006.

COSTS AND EXPENSES

Gross margins for the three months ended March 31, 2006 were $666 thousand, compared to gross margins of $53 thousand for the same period of the prior year or up 1167%. For the nine-months ending March 31, 2006, gross margins increased 315% from $163 thousand to $675 thousand. The increase in gross margin resulted primarily from the significant increase in the Company's net revenue consisting almost entirely of recognition of deferred revenues.

The Company is currently in the process of developing a revised business structure that the Company believes will enhance revenue through

leasing of the Company's products and providing services to the Company's customers rather than direct sales.

General and administrative expenses for the three months ended March 31, 2006 were $162 thousand compared to $23 thousand for the same period last year, an increase of $139 thousand or 591%. The increase primarily reflects the accrual of the CEO's salary and full time employment of one person. During the three months ended march 31, 2005 the Company only had part time employees. Since July 2005, the Company's CEO has taken a minimal salary and the balance has been accrued per his contract. This accrual was initiated on April 1, 2005.

Depreciation and amortization expense for the three-month period ended March 31, 2006 decreased $8 thousand from $10 thousand to $2 thousand or a 77% decrease, compared to March 31, 2005. Expenses for the nine-month period ended March 31, 2006 decreased $24 thousand from $28 thousand to $4 thousand or an 86% decrease compared to March 31, 2005.

OPERATING INCOME / LOSS

The Company recorded an operating income for three-months ending March 31, 2006 of $501 thousand, compared to $3 thousand for the same period in 2005 reflecting a change of $498 thousand. The Company recorded an operating income for nine-months ending March 31, 2006 of $191 thousand, compared to an operating loss of $274 thousand for the same period in 2005. The difference of approximately $465 thousand or 169% increase. Increases for the three and nine-month periods ended March 31, 2006 was due principally to the Company's recognition of deferred revenue, increased effort on its reorganization and restructuring, accrued wages and the impairment of BCS inventory.

OTHER INCOME / EXPENSE

Net other income and expense for the three months ended March 31, 2006 reflected a gain of $353 thousand from the same period of 2005, from $5 thousand expense on March 31, 2005 to income of $348 thousand on March 31, 2006. Net other income and expense increased from $14 thousand expense for the nine months ended March 31, 2005 to $331 thousand income March 31, 2006. A major portion of the gain was due to the extinguishment of three debts totaling $359 thousand. Interest expense is primarily an accrual of imputed interest to March 31, 2006 on five loans: $100 thousand with $17,932 accrued interest to March 31, 2006, $200 thousand principal with $21,534 accrued interest to March 31, 2006, $4,981 interest to date on a $100 thousand note and $325 thousand has accrued $12,021 in interest to March 31, 2006. There was one $20,000 related party note which, as of March 31, 2006, has accrued interest of $2,265 from the inception of the loan. Interest income of less than $1 thousand during the period ending March 31, 2006 is also shown.

NET INCOME/(LOSS)

The Company recognized an extraordinary gain during the three and nine-month periods ended March 31, 2006. This gain was due to release of $359 thousand dollars of debt. The Company recorded no income taxes or income tax benefit due to the going concern opinion issued by the Company's auditors. Because the Company's future as an ongoing business is in question, the Company's ability to take advantage of a booked tax benefit is also in question. Therefore, no benefit has been recognized. However, the Company does hope to be

able to, in the future, obtain a profitable operational status at which time the Company could then take advantage of a net operating loss carry-forward for tax purposes.

The net income and loss for the three-month period ended March 31, 2006 resulted in a per share income gain of less than $0.01 and loss of less than $0.01 ending March 31, 2005. For the nine-month period ended March 31, 2006 the Company recognized a per share income gain of less than $0.01 and a loss of less than $0.01 ending March 31, 2005.

LIQUIDITY AND CAPITAL RESOURCES

SOURCES AND USES OF LIQUIDITY

The Company's sources of funds used for operations have historically come from selling common stock, as well as the issuance and exercise of options and warrants, revenues generated from operations, sales of marketable securities, interest earned from marketable securities available for sale and debt assumption.

For the three month period ended March 31, 2006 the Company's sole source of cash was from product sales. The Company is pursuing additional financial transactions and has received $325 thousand as debt proceeds within the past nine-months. As of the date of this report none have been finalized.

The Company's cash requirements include, but are not limited to, general corporate expenses, including employee salaries and benefits, lease payments on office space, legal and accounting fees for litigation and public reporting requirements, procurement of inventory and supply expenses associated with the Company's efforts to manufacture and market its medical and industrial applications. The Company has reduced many of these costs in an effort to preserve cash; however, most of these costs are attributable to activities that are necessary to continue the Company's operations.

Net cash used in operating activities for the nine-months ended March 31, 2006 was $353 thousand, compared to $163 thousand of cash for the nine-months ended March 31, 2005. The increase in cash used in operating activities was primarily a result of the Company's fluctuations in accounts payable, accrued expense balances and deferred revenues.

As of April 1, 2006, the Company's current monthly expense rate averaged $57 thousand during the prior nine-months; the Company's monthly expense rate at its former full operational level was approximately $1.1 million per month.

The Company has no contractual obligations or commitments as of March 31, 2006. All rentals and leases are on a month-to-month basis.

CAPITAL REQUIREMENTS/PLAN OF OPERATION

The Company's capital requirements have varied significantly from the Company's estimates and will likely continue to vary from those estimates. The Company's capital requirements depend upon numerous factors including, but not limited to: a) FDA approval process; b) results of pre-clinical and clinical testing; c) costs of technology; d) time and costs involved in obtaining other

regulatory approvals; e) costs of filing, defending and enforcing any patent claims and other intellectual property rights; f) the economic impact of developments in competing technology and the Company's markets; g) competing technological and market developments; h) the terms of any new collaborative, licensing and other arrangements that the Company may establish; i) litigation costs; and j) costs the Company incurs in responding to inquiries and investigations conducted by the SEC and other governmental entities.

Since inception, the Company has generated significant losses from operations ($97.1 million), but only limited revenues ($4 million). The Company has taken actions to reduce its expenses and cash consumption; however, the Company expects to incur additional operating losses for the indefinite future. The Company's working capital requirements in the foreseeable future will depend on a variety of factors and assumptions. In particular, the Company will need to obtain additional financing through additional equity and/or debt financings or through the sale of assets (including its intellectual property) during fiscal year 2006. If the Company raises additional funds through the issuance of equity securities or other financing instruments which are convertible for equity securities, the Company's shareholders may experience significant dilution that would aversely affect the price of the Company's common stock. Furthermore, there can be no assurance that additional financing will be available when needed or at all, or that if available, such financing will be on terms favorable to the Company or its shareholders. If financing is not available when required or is not available on acceptable terms, the Company may be required to curtail the operating plan and will likely not be able to continue operations as a going concern.

The Company does not have sufficient capital to cover: 1) the expected costs of additional clinical studies currently required by the FDA; or 2) the anticipated expense of funding the Company's business plan over the next year. The Company will not be able to continue its business operations unless the Company obtains additional capital immediately. This capital, if obtained, could be generated through issuance of securities, assumption of loans, and sale of assets (including intellectual property); however, the Company has only limited commitments for any capital infusion, and can give no assurance that the Company will be able to raise any such capital. Furthermore, the Company's troubled financial condition, as well as the lack of FDA pre-market approval of the BCS2100, has made it difficult if not impossible to raise capital needed to continue the Company's operations. If the Company is not successful in quickly raising additional capital, the Company will have to further scale back its business plan or discontinue operations.

As of March 31, 2006, the Company believed that the Company had sufficient liquidity to sustain the current level of limited operations for the next two months. The Company's monthly expense rate at that time averaged $57 thousand. The Company had cash, marketable securities and pre-paid expenses of approximately $115 thousand and current liabilities (excluding the debenture and deferred revenue) of approximately $1.6 million. On a short-term basis, the Company believes it will be able to fund the current level of limited operations

with cash on hand and the proceeds of its receivables and current sales activities; however, to fund the Company's operations over the long term (more than 2 months) the Company believes additional capital or curtailing the operation will be required.

Overall, the Company has reduced the monthly cash consumption to under $55 thousand, which the Company currently believes will be adequate to sustain its curtailed operations only through May 2006. The Company has systematically reduced expenses by eliminating all expenditures except for those necessary to fill orders, file regulatory reports, and seek funding. If the Company is unable to secure additional capital, the Company will likely be forced to discontinue operations entirely.

ITEM 3. CONTROLS AND PROCEDURES

(a) Based on the evaluation of the Company's "disclosure controls and procedures" (as defined in the Securities Exchange Act of 1934 Rules 13a-15(e) or 15d-15(e)) required by paragraph (b) of Rules 13a-15 or 15d-15, the Company's President and the Acting Chief Financial Officer have concluded that, as of March 31, 2006, the Company's disclosure controls and procedures were effective in ensuring that information required to be disclosed in our reports filed or submitted under the Exchange Act is recorded, processed, summarized and reported as specified in the SEC's rules and forms.

(b) The Company is not presently required to conduct quarterly evaluations of its internal control over financial reporting pursuant to paragraph (d) of Rules 13a-15 or 15d-15 promulgated under the Exchange Act. The Company is, however, in the process of designing, evaluating and implementing internal controls in anticipation of the date when it may become subject to such evaluation requirements.

PART II -- OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

SEC INVESTIGATION

In December 2002, the Company was requested to provide certain documents to the Securities and Exchange Commission (the "Commission") and the U.S. Department of Justice in connection with an investigation regarding possible violations of the insider trading prohibitions found in the federal securities laws. The Company has responded to the Commission's requests for copies of documentation, and members of the Company's management have provided testimony to the Commission. To date, the Company has incurred approximately $650,000 in legal costs in complying with these requests. The Company may also be required to indemnify its officers and directors in connection with fees incurred in connection with these investigations. The Company's efforts to respond to the Commission's requests have required, and in the future may require, significant additional legal expenses, may make fund raising more difficult if not impossible, and will distract the Company's management from day-to-day operations.

INDEMNIFICATION

Under the Company's bylaws and contractual agreements, the Company may be required to indemnify its current and former officers and directors who are parties to litigation or other proceedings by providing legal defense through the Company's attorneys (or reimbursing the parties for their own attorneys) and covering all damages the parties may suffer if the plaintiffs are successful.

OTHER LEGAL PROCEEDINGS

The Company is involved in certain other litigation matters in the normal course of business which the Company's management currently believes is not likely to result in any material adverse effects on the Company's financial position, results of operations, or net cash flows.

ITEM 2. EXHIBITS

31.1	Certification of Chief Executive Officer
31.2	Certification of Chief Financial Officer
32.1	Certification of Chief Executive Officer
32.2	Certification of Chief Financial Officer

SIGNATURES

In accordance with the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

COMPUTERIZED THERMAL IMAGING, INC.

Dated May 15, 2006

/s/ Richard V. Secord

Richard V. Secord
Chairman of the Board and
Chief Executive Officer