

Edgar Filing: ICAD INC - Form 8-K/A

ICAD INC  
Form 8-K/A  
March 15, 2004

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 8-K/A

CURRENT REPORT

Pursuant to Section 13 or 15 (d) of the  
Securities Exchange Act of 1934

Date of Report (Date of earliest event reported): December 31, 2003  
-----

iCAD, INC.  
-----

(Exact name of registrant as specified in its charter)

|   |  |   |
|---|--|---|
| Delaware<br>-----<br>(State or other<br>jurisdiction of<br>incorporation) | 1-9341<br>-----<br>(Commission<br>File Number) | 02-0377419<br>-----<br>(IRS Employer<br>Identification No.) |
|---|--|---|

4 Townsend West, Suite 17, Nashua, NH 03063  
-----  
(Address of principal executive offices) (zip code)

Registrant's telephone number, including area code (603) 882-5200  
-----

-----  
(Former name or former address, if changed since the last report)

ITEM 7. FINANCIAL STATEMENTS AND EXHIBITS

(a) Financial Statements of Business Acquired

Qualia Computing, Inc. and Subsidiaries

Fiscal Year ended March 31, 2003

Financial Page No.  
-----

|   |   |
|---|---|
| Report of Independent Auditors                            | 1 |
| Consolidated Balance Sheet                                | 2 |
| Consolidated Statements of Operations                     | 3 |
| Consolidated Statement of Comprehensive Loss              | 4 |
| Consolidated Statement of Changes in Stockholders' Equity | 5 |
| Consolidated Statement of Cash Flows                      | 6 |

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|  |      |
|--|------|
| Notes to Consolidated Financial Statements                             | 7-14 |
| Independent Auditors' Report on Consolidated Supplementary Information | 15   |
| Consolidated Schedule of Selling, General and Administrative Expenses  | 16   |

Nine Months Ended December 31, 2003

|  |      |
|--|------|
| Report of Independent Auditors   | 1    |
| Consolidated Balance Sheet   | 2    |
| Consolidated Statement of Operations                                   | 3    |
| Consolidated Statement of Changes in Stockholders' Equity              | 4    |
| Consolidated Statement of Cash Flows                                   | 5    |
| Notes to Consolidated Financial Statements                             | 6-13 |
| Independent Auditors' Report on Consolidated Supplementary Information | 14   |
| Consolidated Schedule of Selling, General and Administrative Expenses  | 15   |

(b) Pro forma financial information.

|   |         |
|---|---------|
| Unaudited Pro Forma Combined Condensed Balance Sheet as of September 30, 2003                               | PF1-PF2 |
| Unaudited Pro Forma Combined Condensed Statement of Operations for year ended December 31, 2002             | PF3     |
| Unaudited Pro Forma Combined Condensed Statement of Operations for the Nine Months ended September 30, 2003 | PF4     |
| Notes to Pro Forma Combined Condensed Financial Statements  | PF5-PF7 |

(c) Exhibits

23.1 Consent of Brady Ware & Schoenfeld, Inc.

QUALIA COMPUTING, INC. AND SUBSIDIARIES

CONSOLIDATED FINANCIAL STATEMENTS

YEAR ENDED MARCH 31, 2003

QUALIA COMPUTING, INC. AND SUBSIDIARIES

TABLE OF CONTENTS

YEAR ENDED MARCH 31, 2003

-----

Page

----

## Edgar Filing: ICAD INC - Form 8-K/A

|  |      |
|--|------|
| INDEPENDENT AUDITORS' REPORT   | 1    |
| FINANCIAL STATEMENTS   |      |
| Consolidated Balance Sheet   | 2    |
| Consolidated Statement of Operations                                   | 3    |
| Consolidated Statement of Comprehensive Loss                           | 4    |
| Consolidated Statement of Changes in Stockholders' Equity              | 5    |
| Consolidated Statement of Cash Flows                                   | 6    |
| Notes to Consolidated Financial Statements                             | 7-14 |
| SUPPLEMENTARY INFORMATION  |      |
| Independent Auditors' Report on Consolidated Supplementary Information | 15   |
| Consolidated Schedule of Selling, General and Administrative Expenses  | 16   |

Pushing the Possibilities

[BRADY WARE LOGO]

### INDEPENDENT AUDITORS'REPORT

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One South Main Street  
Suite 600  
Dayton, Ohio 45402  
(937) 223-5247  
(800) 893-4283  
Fax (937) 223-0300

Board of Directors  
Qualia Computing and Subsidiaries  
Beavercreek, Ohio

One Woodside Drive  
Richmond, Indiana 47374  
(765) 966-0531  
(800) 515-5536  
Fax (765) 962-5015

[www.bradyware.com](http://www.bradyware.com)

We have audited the accompanying consolidated balance sheet of QUALIA COMPUTING, Inc. and Subsidiaries as of March 31, 2003, and the related consolidated statements of operations, comprehensive loss, changes in stockholders' equity and cash flows for the year then ended. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. 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

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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, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Qualia Computing, Inc. and Subsidiaries as of March 31, 2003, and the results of its operations and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

/s/ BRADY WARE & SCHOENFELD, INC.

-----  
Dayton, Ohio  
August 26, 2003

1

### QUALIA COMPUTING, INC. AND SUBSIDIARIES

#### CONSOLIDATED BALANCE SHEET

MARCH 31, 2003

-----  
ASSETS

CURRENT ASSETS

|                           |    |           |
|---------------------------|----|-----------|
| Cash and cash equivalents | \$ | 2,339,669 |
| Accounts receivable       |    | 2,632,643 |
| Inventory                 |    | 1,742,234 |
| Prepaid expenses          |    | 213,602   |
| Prepaid income taxes      |    | 64,250    |
| Investments               |    | 256,729   |

-----  
7,249,127

PROPERTY AND EQUIPMENT, NET 1,020,956

OTHER ASSETS 565,449

-----  
\$ 8,835,532  
=====

#### LIABILITIES AND STOCKHOLDERS' EQUITY

CURRENT LIABILITIES

|                  |    |         |
|------------------|----|---------|
| Accounts payable | \$ | 596,063 |
| Accrued expenses |    | 766,952 |

-----  
1,363,015  
-----

STOCKHOLDERS' EQUITY

|                                   |  |        |
|-----------------------------------|--|--------|
| Common stock                      |  | 15     |
| Cumulative translation adjustment |  | 27,498 |

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|  |              |
|--|--------------|
| Paid-in capital                        | 36,260,994   |
| Accumulated deficit                    | (28,817,326) |
| Accumulated other comprehensive income | 1,336        |
|  | -----        |
|  | 7,472,517    |
|  | -----        |
|  | \$ 8,835,532 |
|  | =====        |

See notes to financial statements. 2

QUALIA COMPUTING, INC. AND SUBSIDIARIES  
CONSOLIDATED STATEMENT OF OPERATIONS  
YEAR ENDED MARCH 31, 2003

|  |                 |
|--|-----------------|
| NET SALES                                    | \$ 5,092,340    |
| COST OF SALES                                | 2,216,179       |
|  | -----           |
| GROSS MARGIN                                 | 2,876,161       |
| SELLING, GENERAL AND ADMINISTRATIVE EXPENSES | 9,829,308       |
|  | -----           |
| LOSS FROM OPERATIONS                         | (6,953,147)     |
| OTHER INCOME (EXPENSE) - NET                 | 215,772         |
|  | -----           |
| LOSS BEFORE INCOME TAXES                     | (6,737,375)     |
| INCOME TAX EXPENSE                           | (8,759,473)     |
|  | -----           |
| NET LOSS                                     | \$ (15,496,848) |
|  | =====           |

See notes to financial statements. 3

QUALIA COMPUTING, INC. AND SUBSIDIARIES  
CONSOLIDATED STATEMENT OF COMPREHENSIVE LOSS  
YEAR ENDED MARCH 31, 2003

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|  |                 |
|--|-----------------|
| NET LOSS                                 | \$ (15,496,848) |
| OTHER COMPREHENSIVE LOSS                 |                 |
| Unrealized gain on investment securities | 163             |
|  | -----           |
| COMPREHENSIVE LOSS                       | \$ (15,496,685) |
|  | =====           |

See notes to financial statements. 4

QUAUA COMPUTING, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENT OF CHANGES IN STOCKHOLDERS' EQUITY

YEAR ENDED MARCH 31, 2003

|   | COMMON<br>STOCK | PREFERRED<br>STOCK | PREFERRED<br>STOCK<br>SUBSCRIBED | CUMULATIVE<br>Translation<br>Adjustments | PAID<br>CAPITAL |
|---|-----------------|--------------------|----------------------------------|--|-----------------|
|   | -----           | -----              | -----                            | -----                                    | -----           |
| Balance - March 31, 2002                                  | \$ 8,470        | \$ 193             | \$ 1,350,000                     | \$ -                                     | \$23,353        |
| Net loss  | -               | -                  | -                                | -  |                 |
| Sale of treasury stock                                    | -               | -                  | -                                | -  |                 |
| Unrealized gain on investments                            | -               | -                  | -                                | -  |                 |
| Gain on translation of currency                           | -               | -                  | -                                | 37,200                                   |                 |
| Issuance of 3,000 shares of common stock                  | -               | -                  | -                                | -  | 3               |
| Issuance of 1,350 preferred shares, previously subscribed | -               | 13                 | (1,350,000)                      | -  | 1,350           |
| Issuance of 2,075 preferred shares                        | -               | 21                 | -                                | -  | 5,997           |
| Recapitalization/acquisition of subsidiaries              | (8,455)         | (227)              | -                                | (9,702)                                  | 5,556           |
|   | -----           | -----              | -----                            | -----                                    | -----           |
| Balance - March 31, 2003                                  | \$ 15           | \$ -               | \$ -                             | \$ 27,498                                | \$36,260        |
|   | =====           | =====              | =====                            | =====                                    | =====           |

| TREASURY<br>STOCK | ACCUMULATED<br>OTHER<br>COMPREHENSIVE<br>INCOME | ACCUMULATED<br>DEFICIT | TOTAL<br>STOCKHOLDERS<br>EQUITY (DEFICI |
|-------------------|---|------------------------|---|
| -----             | -----   | -----                  | -----                                   |

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|   |              |          |                 |             |
|---|--------------|----------|-----------------|-------------|
| Balance - March 31, 2002                                  | \$ (350,000) | \$ 1,173 | \$ (13,026,478) | \$ 11,337,2 |
| Net loss  | -            | -        | (15,496,848)    | (15,496,8   |
| Sale of treasury stock                                    | 350,000      | -        | (294,000)       | 56,0        |
| Unrealized gain on investments                            | -            | 163      | -               | 1           |
| Gain on translation of currency                           | -            | -        | -               | 37,2        |
| Issuance of 3,000 shares of common stock                  | -            | -        | -               | 3,0         |
| Issuance of 1,350 preferred shares, previously subscribed | -            | -        | -               |             |
| Issuance of 2,075 preferred shares                        | -            | -        | -               | 5,997,2     |
| Recapitalization/acquisition of subsidiaries              | -            | -        | -               | 5,538,5     |
|   | -----        | -----    | -----           | -----       |
| Balance - March 31, 2003                                  | \$ -         | \$ 1,336 | \$ (28,817,326) | \$ 7,472,5  |
|   | =====        | =====    | =====           | =====       |

See notes to financial statements.

5

QUALIA COMPUTING, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENT OF CASH FLOWS

YEAR ENDED MARCH 31, 2003

OPERATING ACTIVITIES

|   |                 |
|---|-----------------|
| Net loss  | \$ (15,496,848) |
| Adjustments to reconcile net loss to not cash used by operating activities: |                 |
| Depreciation and amortization   | 419,393         |
| Deferred income taxes   | 8,762,889       |
| Cumulative translation adjustments  | 37,200          |
| Inventory reserve   | 100,000         |
| Allowance for doubtful accounts   | 930,000         |
|   | -----           |
|   | (5,247,366)     |
| Changes in operating assets and liabilities:                                |                 |
| Accounts receivable   | 551,187         |
| Inventory   | 328,219         |
| Prepaid expenses  | (63,538)        |
| Other assets  | (85,377)        |
| Accounts payable  | 253,412         |
| Accrued expenses  | (7,404)         |
|   | -----           |
| Net cash used by operating activities                                       | (4,270,867)     |
|   | -----           |

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|  |              |
|--|--------------|
| INVESTING ACTIVITIES                         |              |
| Proceeds from sale of assets                 | 14,282       |
| Purchases of property and equipment          | (389,164)    |
| Purchase of investments                      | (7,528)      |
| Inventory deposits                           | 38,182       |
| Note receivable - related party              | (1,000,000)  |
| Cash received in acquisition of subsidiaries | 188,714      |
|  | -----        |
| Net cash used by investing activities        | (1,155,514)  |
|  | -----        |
| FINANCING ACTIVITIES                         |              |
| Issuance of common stock                     | 3,000        |
| Issuance of preferred stock                  | 5,997,227    |
| Sale of treasury stock                       | 56,000       |
|  | -----        |
| Net cash provided by financing activities    | 6,056,227    |
|  | -----        |
| NET INCREASE IN CASH AND CASH EQUIVALENTS    | 629,846      |
| CASH AND CASH EQUIVALENTS                    |              |
| Beginning of year                            | 1,709,823    |
|  | -----        |
| End of year                                  | \$ 2,339,669 |
|  | =====        |

See notes to financial statements.

6

QUALIA COMPUTING, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE A - COMPANY OPERATIONS AND FINANCIAL VIABILITY

QUALIA COMPUTING, INC. AND SUBSIDIARIES is a software research and development organization specializing in computer-aided intelligence amplification, with applications in the fields of human decision making, including computer-aided cancer detection, intelligent drug and vaccine discovery, text categorization and time-series prediction. The Company's market is global with its headquarters located in Dayton, Ohio. The Company incurred research and development costs of \$2,838,490 during the year.

During September 2002, Qualia Computing, Inc. acquired the subsidiaries of Cadx Systems, Inc (Cadx USA), Cadx Medical Systems Inc (Cadx Canada), Cadx Medical Systems Limited (Cadx Ireland), and Cadx Medical Systems SARL (Cadx France) in exchange for giving Cadx Canada Inc. (owned by Shire Pharmaceuticals) 138,164 additional Qualia Computing, Inc. class B shares to bring their total ownership to 50%. The operations of the subsidiaries is being reported from September 26, 2002 through March 31, 2003.

Prior to the recapitalization of the capital (See Note M), the Company had been funding its operations with the sale of preferred shares of stock to Cadx Canada Inc. (Shire Pharmaceuticals). This capital was to be used to finance operations



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until an investor could be found to acquire Shire's shares- As of the date of these financial statements, investors have been found and negotiations are taking place. (See Note Q). As part of the acquisition of these shares, the investors intend to contribute \$10 million in cash to finance operations.

### NOTE B - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

**PRINCIPLES OF CONSOLIDATION** - The accompanying consolidated financial statements include the accounts of Qualia Computing, Inc. and its wholly owned subsidiaries, Cadx Systems, Inc (Cadx USA), Cadx Medical Systems Inc (Cadx: Canada), Cadx Medical Systems Limited (Cadx Ireland), and Cadx Medical Systems SARL (Cadx France). All significant inter-company transactions and balances have been eliminated in the accompanying consolidated financial statements.

**FINANCIAL ESTIMATES** - The preparation of consolidated 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 disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

**REVENUE RECOGNITION** - Sales revenue is recognized at the time title changes. A technician installs the unit after shipment, however, the cost associated with the installation is de minimis. Contract service revenue is recognized over the life of the contract. The unearned revenue is accounted for in the balance sheet account, "deferred revenue."

**CONCENTRATIONS** - Financial instruments that potentially subject the Company to credit risk consist principally of trade accounts receivable. In addition, from time to time, the Company has funds on deposit with a financial institution in excess of FDIC insurance limits.

**ACCOUNTS RECEIVABLE** - The Company uses the allowance method for receivables. An allowance for doubtful accounts is established to give recognition to the receivable amounts that may become uncollectible in the future. The allowance is reviewed annually to determine that the amount is appropriate. The allowance for the year ended March 31, 2003 was \$100,000.

7

### QUALIA COMPUTING, INC. AND SUBSIDIARIES

#### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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### NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - continued

**INVENTORIES** - Inventories are valued at the lower of cost (first-in, first-out method) or market. An Inventory reserve of \$100,000 has been set up as of March 31, 2003 to account for future obsolescence.

**PROPERTY AND EQUIPMENT** - PROPERTY and equipment are stated at cost and depreciated over their estimated useful lives using both straight-line and accelerated methods. Routine repairs and maintenance are charged to expense when incurred. Renewals and betterments which substantially increase the life of the property and equipment are capitalized. At retirement or sale, the costs of the assets, less related accumulated depreciation or amortization, are removed from the accounts and resulting gains and losses are included in income.

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INVESTMENTS - The Company classifies its marketable equity securities as available for sale. Securities classified as available for sale are carried in the financial statements at fair value. Realized gains and losses, determined using the first-in, first-out (FIFO) method, are included in earnings. Unrealized holding gains and losses are reported in other comprehensive income.

CASH EQUIVALENTS - Cash equivalents include amounts in money market funds and financial instruments with a maturity of less than three months at the date of purchase.

PATENTS - The costs associated with the registration of new patents are being amortized over a period of 15 years. The amortization expense for the year ended March 31, 2003 was \$15,274.

INCOME TAXES - The Company utilizes the asset and liability approach to accounting for income taxes. The objective of the asset and liability method is to establish deferred tax assets and liabilities for temporary differences between the financial reporting and the tax bases of the Company's assets and liabilities at enacted tax rates expected to be in effect when such amounts are realized or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date.

ADVERTISING EXPENSE - ADVERTISING costs are expensed as incurred. Advertising expense was \$280,468 for the year ended March 31, 2003.

NOTE C - ACCOUNTS RECEIVABLE

|               |              |
|---------------|--------------|
| Trade         | \$ 2,553,201 |
| Employees     | 36,002       |
| Miscellaneous | 43,440       |
|               | -----        |
|               | \$ 2,632,643 |
|               | =====        |

8

QUALIA COMPUTING, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE D - INVENTORY

|                   |              |
|-------------------|--------------|
| Finished goods    | \$ 1,308,214 |
| Parts             | 534,020      |
| Inventory reserve | (100,000)    |
|                   | -----        |
|                   | \$ 1,742,234 |
|                   | =====        |

NOTE E - INVESTMENTS

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The following table reflects the cost and estimated fair values of equity securities held at March 31, 2003. In addition, gross unrealized gains and losses are disclosed as of March 31, 2003.

|                   | Gross<br>Unrealized<br>Gains | Gross<br>Unrealized<br>Losses | Estimated Fair<br>Value |
|-------------------|------------------------------|-------------------------------|-------------------------|
| COST              | Gains                        | Losses                        | Value                   |
| -----             | -----                        | -----                         | -----                   |
| Equity securities | \$ 255,393                   | \$ 1,336                      | \$ -                    |
|                   | =====                        | =====                         | =====                   |

Realized gains and losses for securities classified as available-for-sale are reported in earnings based on the adjusted cost of the specific security sold. There were no sales of securities for the year ended March 31, 2003.

### NOTE F - PROPERTY AND EQUIPMENT

|  |              |
|--|--------------|
| Leasehold improvements                         | \$ 54,431    |
| Furniture, fixtures, and equipment             | 423,401      |
| Computer equipment                             | 171,828      |
| Research equipment                             | 1,344,348    |
| Software                                       | 263,678      |
|  | -----        |
| Total cost                                     | 2,257,686    |
| Less accumulated depreciation and amortization | 1,236,730    |
|  | -----        |
|  | \$ 1,020,956 |
|  | =====        |

### NOTE G - OTHER ASSETS

|  |            |
|--|------------|
| Deposits                               | \$ 166,007 |
| Cash surrender value of life insurance | 13,501     |
| Patent cost                            | 253,677    |
| Accumulated amortization - patents     | (37,736)   |
| Note receivable - related party        | 170,000    |
|  | -----      |
|  | \$ 565,449 |
|  | =====      |

9

### QUALIA COMPUTING, INC. AND SUBSIDIARIES

#### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

-----

The note receivable of \$1,000,000 as of March 31, 2003 is due in full on December 31, 2007, Interest is being charged at the prime rate as identified by the bank (4-25% as of March 31, 2003) and is due annually on August 21, the anniversary date of the note. An allowance for doubtful accounts of \$830,000 has been recorded against this note as of March 31, 2003.

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NOTE H - ACCRUED EXPENSES

|   |    |         |
|---|----|---------|
| Wages, bonuses, and commissions                         | \$ | 311,204 |
| Vacation  |    | 92,966  |
| Payroll taxes   |    | 66,306  |
| 401 K and profit sharing                                |    | 132,588 |
| Personal property, sales, and other miscellaneous taxes |    | 14,788  |
| Warranty reserve  |    | 140,600 |
| Deferred revenue  |    | 8,500   |
|   |    | -----   |
|   | \$ | 766,952 |
|   |    | =====   |

The Second Look machines are under warranty for one year. The warranty reserve is based on the costs to cover the labor and the travel costs associated with the warranty service. All parts are under manufactures warranty for a year.

NOTE I - OPERATING LEASES

The Company leases its facilities for \$32,960 per month, The lease expires in December 2010. The Company is also responsible for utilities, real estate taxes, common area maintenance, cleaning and security. The lease amount increases annually throughout the life of the lease. The lease may be renewed for two additional terms of five years each. In connection with this lease, the Company is paying an additional \$1,727 per month for additional build out costs incurred by the lessor for the Company.

The Company also leases additional equipment and storage space as needed during the year.

The lease expense for the year ended March 31, 2003 was \$524,784.

Future minimum lease payments are as follows:

|            |    |           |
|------------|----|-----------|
| 2004       | \$ | 419,212   |
| 2005       |    | 431,166   |
| 2006       |    | 438,298   |
| 2007       |    | 435,438   |
| 2008       |    | 448,501   |
| Thereafter |    | 1,302,600 |
|            |    | -----     |
|            | \$ | 3,475,215 |
|            |    | =====     |

QUALIA COMPUTING, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE J - RELATED PARTY TRANSACTIONS

During the year, the Company engaged non-employee stockholders in consulting

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agreements to perform work on behalf of the Company. The total consulting fees paid under these agreements was \$228,487 for the year ended March 31, 2003.

The Company has a note receivable due from a related party in the amount of \$1,000,000 at March 31, 2003 (see Note G). An allowance for doubtful accounts of \$830,000 has been recorded against this note as of March 31, 2003.

### NOTE K - 401 (K) PLAN

The Company sponsors a contributory defined contribution pension plan as defined by IRS Code Section 401(k). All employees who have attained 21 years of age are eligible to participate in the plan. The Company will match 50% of the first 6% of each employee's wages deferred. An employee is vested in these matching and discretionary funds on a schedule of 20% each year until fully vested after completing five years of service with the Company. At the discretion of the board of directors, the Company may make discretionary contributions to the plan. Total matching and discretionary contributions made by the Company for the year ended March 31, 2003 amounted to \$312,073.

### NOTE L - INCOME TAXES

The Company provides income taxes on items included in the statement of operations regardless of the period when such taxes were payable. Deferred income taxes result from timing differences in the recognition of income and expense for tax and financial statement purposes.

Income tax expense differs from the amount currently payable because income is reported in the statement of operations in periods which differed from those in which they were subject to taxation. These timing differences result principally from net operating loss carryforwards and research and development credit carryforwards. The differences between income tax expense and taxes currently payable are reflected in deferred tax accounts in the balance sheets.

The Income tax provision consists of the following:

|                                   |              |
|-----------------------------------|--------------|
| Current federal tax benefit       | \$ (3,416)   |
| Deferred federal tax benefit      | (2,772,044)  |
| Net change in valuation allowance | 11,534,933   |
|                                   | -----        |
| Income tax expense                | \$ 8,759,473 |
|                                   | =====        |

Components of the deferred tax accounts are as follows:

|                                     |              |
|-------------------------------------|--------------|
| Total long-term deferred tax assets | 11,534,933   |
| Net change in valuation allowance   | (11,534,933) |
|                                     | -----        |
| Net deferred tax asset              | \$ -         |
|                                     | =====        |

The Company has loss carryforwards totaling \$25,897,482 that may be offset against future taxable income, which expire beginning in 2013 through 2023. The Company has research tax credits totaling \$1,461,298

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### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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#### NOTE L - INCOME TAXES - CONTINUED

which expire beginning in 2013 through 2023. The Company also has a capital loss carryforward totaling \$3,644 that may be offset against future capital gains, If not used, the capital loss carryforward will expire in 2004. The deferred tax asset increased to \$11,534,933 in 2003 because of additional net operating loss carryforwards and research credits. Management now believes it is more likely than not that the deferred tax asset will not be realized due to ownership changes which could limit the loss carryforwards available. Accordingly, in 2003, a valuation allowance of \$11,534,933 was provided through charges of \$11,534,933 to the deferred tax provision.

#### NOTE M - STOCKHOLDERS' EQUITY

On September 26, 2002, Qualia Computing entered into a recapitalization agreement with Cadx Canada Inc. (owned by Shire Pharmaceuticals) to restructure the capital of the Company. In the recapitalization. two classes of common shares were defined, Class A and Class B. Cadx Canada Inc. owned all the preferred shares of Qualia Computing, Inc, prior to the recapitalization. These preferred shares were exchanged 1 for 1 for Class B common shares at the recapitalization. At the recapitalization, Qualia Computing, Inc. acquired the subsidiaries of Cadx Systems, Inc (Cadx USA), Cadx Medical Systems Inc (Cadx Canada), Cadx Medical Systems Limited (Cadx Ireland), and Cadx Medical Systems SARL (Cadx France) in exchange for giving Cadx Canada Inc. 138,164 additional Qualia Computing, Inc. Class B shares to bring their total ownership to 50%. The investment in the subsidiaries was recorded at the fair market value of the net assets at the time of the recapitalization.

As of March 31, 2003, the following shares of stock were authorized, issued and outstanding:

|  | Authorized | IS&W    | Outstanding |
|--|------------|---------|-------------|
|  | -----      | -----   | -----       |
| Common shares (Class A, \$.0001 par value) | 1,905,554  | 730,000 | 730,000     |
| Common shares (Class B \$.0001 par value)  | 952,777    | 730,000 | 730,000     |

Class A and B shares have voting rights and are entitled to receive dividends pro rata. Class B shares shall upon a triggering event, be converted without cost into class A shares. Also, upon a triggering event, all stock options exercisable into Class B shares shall be converted automatically into the right to exercise Class A shares. A triggering event shall include a merger, consolidation, reorganization, recapitalization, or any sale, lease, assignment or transfer of all or substantially all assets of the Company.

#### NOTE N - STOCK OPTIONS

The Company initiated a stock option plan approved by the stockholders in February 2001. All options issued to date vest in equal installments over a period of four years with the first installment beginning twelve months following the date of grant. The compensation committee, as delegated by the board, determines the vesting schedule of the options. Prior to September 2002, the term of each option could not exceed ten years from the date of the grant of the option. During September 2002, the plan was amended to have no expiration date. The number of shares of Class A shares available for options is 222,777. The number of shares of Class B shares available for options is

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222,777. The option plan does not allow the issuance of options in an aggregate amount that would result in the outstanding options being greater than 10% of the total number of Class A and B shares outstanding at the time of the option grant.

12

QUALIA COMPUTING, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE N - STOCK OPTIONS - CONTINUED

Stock option activity is presented as follows:

|                         | Optioned<br>Shares<br>(Class A) | Option Price<br>per Share | Total      |
|-------------------------|---------------------------------|---------------------------|------------|
| Balance, March 31, 2002 | 50,700                          | \$ 1.00                   | \$ 50,700  |
| Options issued          | 74,600                          | 1.00                      | 74,600     |
| Balance, March 31, 2003 | 125,300                         | 1.00                      | \$ 125,300 |

The Company did not record an expense for the options issued during the year. If the Company had used fair value based method of accounting for its employee stock option plan, as prescribed by Statement of Financial Accounting Standards No. 123, compensation cost in net loss for the year ended March 31, 2003 would have increased by \$74,600 with a corresponding increase in paid-in capital. Net loss for the year ended March 31, 2003 would have been \$15,571,448.

NOTE O - SPIN OFF

Qualia Financial Services, LLC was spun off from Qualia Computing, Inc. August 21, 2002. Hardware and software, along with cash of \$500,000 and licensed technology for use in online commodities trading of NASDAQ 100 and S & P 500 futures were transferred from Qualia Computing, Inc. in exchange for a promissory note for \$1,000,000. See Note G.

NOTE P - CONTINGENCIES

The Company is involved in a lawsuit with another company over patent infringement. The case has not been settled and no amounts have been accrued as of the date of these financial statements,

NOTE Q - SUBSEQUENT EVENTS

The shareholder who owns the Class B shares is currently in negotiations with individuals concerning the purchase of these Class 8 shares. A letter of intent has been signed as of the date of this report. As part of the purchase of these shares, these individuals intend to contribute cash of approximately \$10 million to the Company.

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The Company has signed agreements with GE to distribute the digital and analog digital products and with Source One to distribute the analog products. With the completion of these two agreements, it is the Company's intent to use distributors as the primary sales vehicle, however, the Company has retained the right to execute direct sales activities as necessary to achieve revenue targets.

One of the subsidiaries, Cadx France, is in the process of being dissolved. Any remaining assets after dissolution will be retained by the parent. No estimates can be made as to the effect of this item on the financial statements.

13

### QUALIA COMPUTING, INC. AND SUBSIDIARIES

#### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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##### NOTE R - FOREIGN CURRENCY ITEMS

Cadx Canada, Cadx France and Cadx Ireland transacted a portion of their business using foreign currency. The transactions have been recorded in accordance with FASB 52 using the current rate of exchange, as applicable, on the transaction date. Gains or losses from the settlement of the foreign currency transactions are reported in other income (expense), as applicable on the payment date.

Foreign currency losses amounting to \$7,593 have been reported in the other income (expense) for the year ended March 31, 2003.

Cadx Canada, Cadx France, and Cadx Ireland use foreign currency as their functional currency. Translation adjustments result from the process of translating those entities' financial statements into the reporting currency of Qualia Computing. In accordance with FASB 52, those translation adjustments are not included in determining net income but are reported separately and accumulated in a separate component of equity called cumulative translation adjustments.

##### NOTE S - SUPPLEMENTAL CASH FLOW INFORMATION

Cash paid during the year for

|               |    |       |
|---------------|----|-------|
| Interest paid | \$ | 185   |
|               |    | ===== |

Non cash investing and financing activities:

Acquisition of subsidiaries

|                                  |    |             |
|----------------------------------|----|-------------|
| Cash received                    | \$ | 188,714     |
| Accounts receivable              |    | 3,104,649   |
| Inventory                        |    | 2,315,899   |
| Property and equipment           |    | 480,852     |
| Other assets                     |    | 35,901      |
| Accounts payable assumed         |    | (46,447)    |
| Accrued expenses assumed         |    | (532,382)   |
| Cumulated translation adjustment |    | 9,702       |
| Equity                           |    | (5,556,888) |
|                                  |    | -----       |

|                                       |    |       |
|---------------------------------------|----|-------|
| Cash paid to acquire the subsidiaries | \$ | -     |
|                                       |    | ===== |



Pushing the Possibilities

[BRADY WARE LOGO]

INDEPENDENT AUDITORS' REPORT ON CONSOLIDATED  
SUPPLEMENTARY INFORMATION

One South Main Street  
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Dayton, Ohio 45402  
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Board of Directors  
QUALIA COMPUTING, INC. AND SUBSIDIARIES  
Beavercreek, Ohio

One Woodside Drive  
Richmond, Indiana 47374  
(765) 966-0531  
(800) 515-5536  
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www.bradyware.com

Our report on our audit of the basic financial statements of QUALIA COMPUTING, INC. AND SUBSIDIARIES as of March 31, 2003 appears on page one. Our audit was conducted for the purpose of forming an opinion on the basic financial statements taken as a whole. The supplementary information (shown on page 16) is presented for purposes of additional analysis of the financial statements rather than to present the consolidated balance sheet, results of operations and cash flows of the Company. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion is fairly stated in all material respects in relation to the financial statements taken as a whole for the year ended March 31, 2003.

/s/ BRADY WARE & SCHOENFELD, INC.

Dayton, Ohio  
August 26, 2003

QUAUA COMPUTING, INC. AND SUBSIDIARIES

CONSOLIDATED SCHEDULE OF SELLING, GENERAL AND ADMINISTRATIVE EXPENSES

YEAR ENDED MARCH 31, 2003

|                                  |           |
|----------------------------------|-----------|
| Wages                            | 4,416,604 |
| Bonuses                          | 208,045   |
| Payroll taxes                    | 337,795   |
| Employee benefits                | 433,173   |
| 401 (k) match and profit sharing | 312,073   |
| Bank charges                     | 7,239     |
| Computer supplies                | 47,166    |

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|                                     |              |
|-------------------------------------|--------------|
| Repair and maintenance              | 26,195       |
| Consulting fees                     | 490,770      |
| Legal and professional fees         | 737,785      |
| Meals and entertainment             | 146,632      |
| Contributions                       | 25,250       |
| Travel                              | 710,971      |
| Training and seminars               | 28,941       |
| Office expense                      | 63,443       |
| Postage and freight                 | 126,245      |
| Rent                                | 524,784      |
| Research                            | 12,406       |
| Dues and subscriptions              | 27,852       |
| Advertising                         | 280,468      |
| Depreciation expense                | 404,119      |
| Amortization expense                | 15,274       |
| Insurance                           | 75,660       |
| Miscellaneous taxes                 | 56,074       |
| Telephone and utilities             | 120,461      |
| Personal property taxes             | (5,007)      |
| Licenses                            | 37,511       |
| Tuition assistance                  | 11,407       |
| Bad Debt                            | 930,000      |
| Relocation expense                  | 19,252       |
| Expenses allocated to cost of sales | (799,280)    |
|                                     | -----        |
|                                     | \$ 9,829,308 |
|                                     | =====        |

See independent auditors' report on consolidated supplementary information. 16

QUALIA COMPUTING, INC. AND SUBSIDIARIES  
CONSOLIDATED FINANCIAL STATEMENTS  
NINE MONTHS ENDED DECEMBER 31, 2003

QUALIA COMPUTING, INC. AND SUBSIDIARIES

TABLE OF CONTENTS

NINE MONTHS ENDED DECEMBER 31, 2003

-----

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INDEPENDENT AUDITORS' REPORT

FINANCIAL STATEMENTS

Consolidated Balance Sheet

Consolidated Statement of Operations

Consolidated Statement of Changes in Stockholders' Equity

Consolidated Statement of Cash Flows

Notes to Consolidated Financial Statements

SUPPLEMENTARY INFORMATION

Independent Auditors' Report on Consolidated Supplementary Information

Consolidated Schedule of Selling, General and Administrative Expenses

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INDEPENDENT AUDITORS'REPORT

One South Main Street  
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Dayton, Ohio 45402  
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Board of Directors  
QUALIA COMPUTING, INC. AND SUBSIDIARIES  
Beavercreek, Ohio

One Woodside Drive  
Richmond, Indiana 47374  
(765)966-0531  
(800)515-5536  
Fax (765)962-5015

We have audited the accompanying consolidated balance sheet of QUALIA COMPUTING, INC. and Subsidiaries as of December 31, 2003, and the related consolidated statements of operations, changes in stockholders' equity and cash flows for the nine months then ended. These consolidated financial statements are the responsibility of the Company's management. our responsibility is to express an opinion on these consolidated financial statements based on our audit.

www.bradyware.com

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. 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.

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In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Qualia Computing, Inc. and Subsidiaries as of December 31, 2003, and the results of its operations and its cash flows for the nine months then ended in conformity with accounting principles generally accepted in the United States of America.

/s/ BRADY WARE & SCHOENFELD, INC

-----  
Dayton, Ohio  
February 3, 2004

1

### QUALIA COMPUTING, INC. AND SUBSIDIARIES

#### CONSOLIDATED BALANCE SHEET

DECEMBER 31, 2003

#### ASSETS

##### CURRENT ASSETS

|                           |    |           |
|---------------------------|----|-----------|
| Cash and cash equivalents | \$ | 446,031   |
| Accounts receivable       |    | 2,479,089 |
| Inventory                 |    | 1,457,636 |
| Prepaid expenses          |    | 63,523    |
|                           |    | -----     |
|                           |    | 4,446,279 |

PROPERTY AND EQUIPMENT, NET 850,241

OTHER ASSETS 634,592

-----  
\$ 5,931,112

#### LIABILITIES AND STOCKHOLDERS' EQUITY

##### CURRENT LIABILITIES

|                  |    |           |
|------------------|----|-----------|
| Accounts payable | \$ | 2,722,133 |
| Accrued expenses |    | 1,156,678 |
|                  |    | -----     |
|                  |    | 3,878,811 |
|                  |    | -----     |

##### STOCKHOLDERS' EQUITY

|                                    |    |              |
|------------------------------------|----|--------------|
| Common stock                       |    | 17           |
| Cumulative translation adjustments |    | 95,043       |
| Paid-in capital                    |    | 36,488,492   |
| Accumulated deficit                |    | (34,531,251) |
|                                    |    | -----        |
|                                    |    | 2,052,301    |
|                                    |    | -----        |
|                                    | \$ | 5,931,112    |

=====

See notes to financial statements. 2

QUALIA COMPUTING, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENT OF OPERATIONS

NINE MONTHS ENDED DECEMBER 31, 2003

-----

|  |                                 |
|--|---------------------------------|
| NETSALES                                     | \$ 10,325,256                   |
| COST OF SALES                                | 4,990,485                       |
| GROSS MARGIN                                 | -----<br>5,334,771              |
| SELLING, GENERAL AND ADMINISTRATIVE EXPENSES | 10,813,972                      |
| LOSS FROM OPERATIONS                         | -----<br>(5,479,201)            |
| OTHER INCOME (EXPENSE) - NET                 | (234,724)                       |
| LOSS BEFORE INCOME TAXES                     | (5,713,925)                     |
| INCOME TAX EXPENSE                           | -----<br>-                      |
| NET LOSS                                     | -----<br>\$ (5,713.92)<br>===== |

See notes to financial statements. 3

QUALIA COMPUTING, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENT OF CHANGES IN STOCKHOLDERS' EQUITY

NINE MONTHS ENDED DECEMBER 31, 2003

-----

|                         | COMMON<br>STOCK | TRANSLATION<br>ADJUSTMENT | PAID-IN<br>CAPITAL | OTHER<br>COMPREHENSIVE<br>INCOME (LOSS) |
|-------------------------|-----------------|---------------------------|--------------------|---|
|                         | -----           | -----                     | -----              | -----                                   |
| Balance - April 1, 2003 | \$ 15           | \$ 27,498                 | \$ 36,260,994      | \$ 1,336                                |

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|                                 |       |           |               |         |
|---------------------------------|-------|-----------|---------------|---------|
| Net loss                        | -     | -         | -             | -       |
| Unrealized loss on investments  | -     | -         | -             | (1,336) |
| Gain on translation of currency | -     | 67,545    | -             | -       |
| Stock options exercised         | \$ 2  | -         | 227,498       | -       |
| Balance - December 31, 2003     | \$ 17 | \$ 95,043 | \$ 36,488,492 | \$ -    |

See notes to financial statements.

4

QUALIA COMPUTING, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENT OF CASH FLOWS

NINE MONTHS ENDED DECEMBER 31, 2003

OPERATING ACTIVITIES

|   |                |
|---|----------------|
| Net loss  | \$ (5,713,925) |
| Adjustments to reconcile net loss to net cash used by operating activities: |                |
| Depreciation and amortization   | 309,721        |
| Loss on disposal of assets  | 164,325        |
| Loss on sale of investments   | 5,545          |
| Cumulative translation adjustments  | 67,545         |
| Change in inventory reserve   | 1,054,163      |
| Change in allowance for doubtful accounts                                   | 271,557        |
|   | (3,841,069)    |

Changes in operating assets and liabilities:

|                     |           |
|---------------------|-----------|
| Accounts receivable | (118,003) |
| Inventory           | (933,065) |
| Prepaid expenses    | 214,329   |
| Other assets        | (84,372)  |
| Accounts payable    | 2,126,070 |
| Accrued expenses    | 389,726   |

Net cash used by operating activities (2,246-384)

INVESTING ACTIVITIES

|                                     |           |
|-------------------------------------|-----------|
| Purchases of property and equipment | (178,485) |
| Proceeds from sale of investments   | 256,410   |
| Purchase of investments             | (6,564)   |

Net cash provided by Investing activities 71,361

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### FINANCING ACTIVITIES

|   |             |
|---|-------------|
| Issuance of common stock                  | 227,500     |
|   | -----       |
| NET DECREASE IN CASH AND CASH EQUIVALENTS | (1,947,523) |
|   |             |
| CASH AND CASH EQUIVALENTS                 |             |
| Beginning of period                       | 2,339,669   |
|   | -----       |
| End of period                             | \$ 446,031  |
|   | =====       |

See notes to financial statements,

5

### QUALIA COMPUTING, INC. AND SUBSIDIARIES

#### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

---

##### NOTE A - COMPANY OPERATIONS AND FINANCIAL VIABILITY

QUALIA COMPUTING, INC. AND SUBSIDIARIES (the "Company") is a software research and development organization specializing in computer-aided intelligence amplification, with applications in the fields of human decision-making, including computer-aided cancer detection, intelligent drug and vaccine discovery, text categorization and time-series prediction. The Company's market is global with its headquarters located in Dayton, Ohio. The Company incurred research and development costs of \$1,896,896 during the period.

On December 31, 2003, Qualia Computing, Inc, was acquired through a stock purchase by iCad, a Delaware corporation which develops, engineers, and manufactures CAD products in the medical imaging and women's health markets. Qualia Computing, Inc. was merged into Qualia Acquisition Corp., a wholly owned subsidiary of iCad. As a result of the merger, shares of Qualia class A and B common stock were deemed cancelled and converted into shares of iCad common stock, except for class B shares owned by CadX Canada, Inc. (Shire Pharmaceuticals) and class A shares owned by Brianna Biotech, Inc., who received cash and notes in lieu of iCad stock. These consolidated financial statements have been prepared on a basis consistent with prior years and do not reflect any adjustments from the application of purchase accounting.

Since inception, the Company had been funding its operations with the sale of preferred shares of stock to Cadx: Canada Inc. (Shire Pharmaceuticals). As described above, the Company has merged with iCad on December 31, 2003. The principal stockholder of iCad has indicated that he will continue to supply the necessary working capital to enable the Company to continue as a going concern.

##### NOTE B - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

PRINCIPLES OF CONSOLIDATION - The accompanying consolidated financial statements include the accounts of Qualia Computing, Inc. and its wholly owned subsidiaries, Cadx: Systems, Inc (Cadx USA), Cadx Medical Systems, Inc (Cadx Canada), Cadx Medical Systems Limited (Cadx Ireland), and Cadx Medical Systems SARL (Cadx France). All significant inter-company transactions and balances have been eliminated in the accompanying consolidated financial statements. Qualia Computing, Inc., the parent, has a March fiscal tax year end. The subsidiaries all have December tax year ends.

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FINANCIAL ESTIMATES - The preparation of consolidated 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 disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

REVENUE RECOGNITION - Sales revenue on units that are sold through a distributor is recognized upon shipment to the distributor. The distributor has responsibility for installation. The Company is providing training after installation on Source One contracts and on GE contracts of analog units; however, the cost of this training is de minimus and insignificant to the overall sale transaction. Sales revenue on units sold directly by the Company is recognized upon installation. Contract service revenue is recognized over the life of the contract. The unearned revenue is accounted for in the balance sheet account, "unearned revenue."

6

QUALIA COMPUTING, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

---

NOTE 8 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED

CONCENTRATIONS - Financial instruments that potentially subject the Company to credit risk consist principally of trade accounts receivable. In addition, from time to time, the Company has funds on deposit with a financial institution in excess of FDIC insurance limits.

ACCOUNTS RECEIVABLE - The Company uses the allowance method in accounting for bad debts. An allowance for doubtful accounts is established to give recognition to the receivable amounts that may become uncollectible in the future. The allowance is reviewed annually to determine that the amount is appropriate. The allowance as of December 31, 2003 was \$1,400.

INVENTORIES - Inventories are valued at the lower of cost (first-in, first-out method) or market. An inventory reserve of \$1,154,163 has been set up as of December 31, 2003 to account for obsolescence. The inventory reserve increased by \$1,054,163 for the nine months ended December 31, 2003. This accounts for approximately 21 % of the cost of sales for the nine months ended December 31, 2003.

PROPERTY AND EQUIPMENT - Property and equipment are stated at cost and depreciated over their estimated useful lives using both straight-line and accelerated methods. Routine repairs and maintenance are charged to expense when incurred. Renewals and betterments which substantially increase the life of the property and equipment are capitalized. At retirement or sale, the costs of the assets, less related accumulated depreciation or amortization, are removed from the accounts and resulting gains and losses are included in income.

PATENTS - The costs associated with the registration of patents are being amortized over a period of 15 years on a straight-line method. The amortization expense for the nine months ended December 31, 2003 was \$15,229.



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INCOME TAXES - The Company utilizes the asset and liability approach to accounting for income taxes. The objective of the asset and liability method is to establish deferred tax assets and liabilities for temporary differences between the financial reporting and the tax basis of the Company's assets and liabilities at enacted tax rates expected to be in effect when such amounts are realized or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date.

ADVERTISING EXPENSE - Advertising costs are expensed as incurred. Advertising expense was \$779,398 for the nine months ended December 31, 2003.

SHIPPING AND HANDLING EXPENSE - Shipping and handling costs are included in the cost of sales.

WARRANTY EXPENSE - The Companies offer a warranty for one year on the Second Look units which coincides with the warranty offered by the manufacturer. Since substantially all warranty claims submitted to the Company are covered by the manufacturers warranty, no additional warranty reserve has been recorded as of December 31, 2003.

7

QUALIA COMPUTING, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE C - ACCOUNTS RECEIVABLE

|                        |              |
|------------------------|--------------|
| Trade                  | \$ 2,382,904 |
| Employees              | 686          |
| Miscellaneous          | 31,666       |
| Related party (Note J) | 63,833       |
|                        | -----        |
|                        | \$ 2,479,089 |
|                        | =====        |

NOTE D - INVENTORY

|                          |              |
|--------------------------|--------------|
| Finished goods           | \$ 1,640,031 |
| Inventory on consignment | 971,768      |
| Inventory reserve        | (1,154,163)  |
|                          | -----        |
|                          | \$ 1,457,636 |
|                          | -----        |

NOTE E - PROPERTY AND EQUIPMENT

|                                    |           |
|------------------------------------|-----------|
| Leasehold improvements             | \$ 9,729  |
| Furniture, fixtures, and equipment | 201,074   |
| Computer equipment                 | 195,579   |
| Research equipment                 | 1,065,506 |
| Manufacturing equipment            | 219,590   |
| Software                           | 103,119   |

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|  |            |
|--|------------|
| Total cost                                     | 1,792,597  |
| Less accumulated depreciation and amortization | 942,356    |
|  | -----      |
|  | \$ 8501241 |
|  | =====      |

NOTE F - OTHER ASSETS

|   |            |
|---|------------|
| Deposits                                    | \$ 245,414 |
| Premium advance receivable - life insurance | 100,000    |
| Patent cost                                 | 342,143    |
| Accumulated amortization - patents          | (52,965)   |
|   | -----      |
|   | \$ 634,592 |
|   | =====      |

8

QUALIA COMPUTING, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE G - ACCRUED EXPENSES

|   |              |
|---|--------------|
| Wages, bonuses, and commissions                         | \$ 747,291   |
| Vacation  | 91,841       |
| Payroll taxes   | 9,436        |
| 401 K   | 63,543       |
| Personal property, sales, and other miscellaneous taxes | 28,067       |
| Unearned revenue  | 216,500      |
|   | -----        |
|   | \$ 1,156,678 |
|   | =====        |

NOTE H - OPERATING LEASES

The Company leases its facilities for \$32,960 per month. The lease expires in December 2010. The Company is also responsible for utilities, real estate taxes, common area maintenance, cleaning and security. The lease amount increases annually throughout the life of the lease. The lease may be renewed for two additional terms of five years each. In connection with this lease, the Company is paying an additional \$1,727 per month for additional build out costs incurred by the lessor for the Company.

The Company is leasing a copier for \$654 per month. The lease expires in February 2008.

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The Company assumed operating leases for computers leased from Shire Biochem. At the end of the lease, the computers are to be returned to Shire. The lease payment is set in Canadian dollars and varies each month as the number of computers leased varies monthly, The final lease payment is due in February 2005.

The Company also leases additional equipment and storage space as needed during the period. The lease expense for the nine months ended December 31, 2003 was \$382.161. Future minimum lease payments are as follows:

|            |    |           |
|------------|----|-----------|
| 2004       | \$ | 426,494   |
| 2005       |    | 428,211   |
| 2006       |    | 440,039   |
| 2007       |    | 453,005   |
| 2008       |    | 459,171   |
| Thereafter |    | 958,712   |
|            |    | -----     |
|            | \$ | 3,165,632 |
|            |    | =====     |

9

### QUALIA COMPUTING, INC. AND SUBSIDIARIES

#### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

---

##### NOTE I - CUSTOMER LEASES

The Company has entered into leasing arrangements with customers for the lease, with an option to purchase the Second Look units. The lease agreements require the lessees to pay to the Company a percentage of the revenue generated by the units. At the end of the lease, the lessees have the option to purchase the unit for an agreed-upon sales price, less the amount already paid to the company.

##### NOTE J - RELATED PARTY TRANSACTIONS

The Company engaged non-employee stockholders in consulting agreements to perform work on behalf of the Company. The total consulting fees paid under these agreements was \$137,502 for the nine months ended December 31, 2003.

The Company has accounts receivable due from a related party in the amount of \$165,390 at December 31, 2003. An allowance for doubtful accounts of \$101,557 has been recorded against this as of December 31, 2003.

The Company has a note receivable due from a related party in the amount of \$1,000,000 at December 31, 2003. The note is due in full on December 31, 2007. Interest is being charged at the prime rate as identified by the bank (4.00% as of December 31, 2003) and is due annually on August 21, the anniversary date of the note. The note is being reserved for the full amount due to substantial doubt about the ability of the borrower to repay the debt.

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### NOTE K - 401 (K) PLAN

The Company sponsors a contributory defined contribution pension plan as defined by IRS Code Section 401 (k). All employees who have attained 21 years of age are eligible to participate in the plan. The Company will match 50% of the first 6% of each employee's wages deferred. An employee is vested in these matching and discretionary funds on a schedule of 20% each year until fully vested after completing five years of service with the Company. At the discretion of the board of directors, the Company may make discretionary contributions to the plan. Total matching and discretionary contributions made by the Company for the nine months ended December 31, 2003 amounted to \$91,673.

### NOTE L - INCOME TAXES

The Company records a provision for federal income taxes on items included in the statement of operations regardless of the period when such taxes are payable. Deferred income taxes result from timing differences in the recognition of income and expense for tax and financial statement purposes.

The Company has loss carryforwards totaling \$30,316,963 that may be offset against future taxable income, which expire beginning in 2013 through 2023. The Company has research tax credits totaling \$1,650,988 which expire beginning in 2013 through 2023. The Company also has a capital loss carryforward totaling \$3,644 that may be offset against future capital gains. If not used, the capital loss carryforward will expire in 2004. The deferred tax asset increased to \$13,552,233 at December 31, 2003 because of additional net operating loss carryforwards and research credits.

10

## QUALIA COMPUTING, INC. AND SUBSIDIARIES

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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### NOTE L - INCOME TAXES - continued

Management now believes it is more likely than not that the deferred tax asset will not be realized due to ownership changes which will limit a portion of the loss carryforwards available (See Note A). Accordingly, in 2003, a valuation allowance of \$13,552,233 was recorded against the deferred tax asset. No amounts were charged to the provision for federal income taxes for the nine months ended December 31, 2003.

### NOTE M - STOCKHOLDERS' EQUITY

As of December 31, 2003, prior to the acquisition and merger into Qualia Acquisition Corp. (See Note A), the following shares of stock were authorized, issued and outstanding:

|   | AUTHORIZED | ISSUED  |
|---|------------|---------|
|   | -----      | -----   |
| Common shares (Class A, \$.00001 par value) | 1,905,554  | 907,500 |
| Common shares (Class B, \$.00001 par value) | 952,777    | 780,000 |

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Class A and B shares have voting rights and are entitled to receive dividends on a pro rata basis. Class B shares shall upon a triggering event, be converted without cost into class A shares. Also, upon a triggering event, all stock options exercisable into Class B shares shall be converted automatically into the right to exercise Class A shares. A triggering event shall include a merger, consolidation, reorganization, recapitalization, or any sale, lease, assignment or transfer of all or substantially all assets of the Company. The merger as describe in Note A is a triggering event.

NOTE N - STOCK OPTIONS

The Company initiated a stock option plan approved by the stockholders in February 2001. All options issued to date vest in equal installments over a period of four years with the first installment beginning twelve months following the date of grant. The compensation committee, as delegated by the board, determines the vesting schedule of the options. Prior to September 2002, the term of each option could not exceed ten years from the date of the grant of the option. During September 2002, the plan was amended to have no expiration date. The option plan does not allow the issuance of options in an aggregate amount that would result in the outstanding options being greater than 10% of the total number of Class A and B shares outstanding at the time of the option grant. As a condition of the merger as described in Note A, the stock option plan was terminated on December 31, 2003.

Stock option activity is presented as follows:

|                            | OPTIONED<br>SHAMS<br>(CLASS A) | OPTION<br>PRICE<br>PER SHARE |
|----------------------------|--------------------------------|------------------------------|
|                            | -----                          | -----                        |
| Balance, March 31, 2003    | 125,300                        | 1.00                         |
| Options issued             | 52,200                         | 1.00                         |
| Options exercised          | (177,500)                      | 1.00                         |
|                            | -----                          | -----                        |
| Balance, December 31, 2003 | -                              |                              |
|                            | -----                          |                              |

11

QUALIA COMPUTING, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE N - STOCK OPTIONS - CONTINUED

| OPTIONED<br>SHARES | OPTION<br>PRICE |
|--------------------|-----------------|
|--------------------|-----------------|

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|                            | (CLASS B) | PER SHARE | TOTAL    |
|----------------------------|-----------|-----------|----------|
|                            | -----     | -----     | -----    |
| Balance, March 31, 2003    | -         | 1.00      | -        |
| Options issued             | 50,000    | 1.00      | 50,000   |
| options exercised          | (50.00)   | 1.00      | (50,000) |
|                            | -----     |           | -----    |
| Balance, December 31, 2003 | -         |           | -        |
|                            | =====     |           | =====    |

NOTE O - DISTRIBUTION AGREEMENTS

The Company signed an agreement with General Electric Company (GE) in June 2003 to distribute digital and analog digital products. The agreement expires December 31, 2007 with options to renew for one year terms. The Company signed a three year agreement with Source One in September 2003 to distribute analog products. The agreement states that there are minimum targets for each of the three years. If the minimums are not met, the Company has the right to convert the agreement to a nonexclusive agreement or terminate the agreement. With the completion of these two agreements, it is the Company's intent to use distributors as the primary sales vehicle, however, the Company has retained the right to execute direct sales activities as necessary to achieve revenue targets.

NOTE P - ACCELERATED PAYMENT AGREEMENT

The Company has entered into an accelerated payment program with General Electric Capital Corporation (GE Capital). The agreement provides payment to the Company upon shipment of goods to GE as provided in the purchase orders. There is a discount associated with the payment of the invoices to the Company. The discount percentage decreases daily from the date of the shipment until the invoice is paid by GE Capital. The agreement expires in October 2004.

NOTE Q - FOREIGN CURRENCY ITEMS

Cadx Canada, Cadx France and Cadx Ireland transacted a portion of their business using foreign currency. The transactions have been recorded in accordance with FASB 52 using the current rate of exchange, as applicable, on the transaction date. Gains or losses from the settlement of the foreign currency transactions are reported in other income (expense), as applicable on the payment date.

Foreign currency losses amounting to \$56,667 have been reported in the other income (expense) for the nine months ended December 31, 2003.

Cadx Canada, Cadx France, and Cadx Ireland use foreign currency as their functional currency. Translation adjustments result from the process of translating those entities' financial statements into the reporting currency of Qualia Computing, Inc. In accordance with FASB 52, those translation adjustments are not included in determining net income but are reported separately and accumulated in a separate component of equity called cumulative translation adjustments.

12

QUALIA COMPUTING, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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NOTE R - SUPPLEMENTAL CASH FLOW INFORMATION

Cash paid during the nine months for:

|               |    |        |
|---------------|----|--------|
| Interest paid | \$ | 53,579 |
|               |    | =====  |

Noncash investing and financing activities:

|                                    |    |         |
|------------------------------------|----|---------|
| Net book value of assets abandoned | \$ | 164,325 |
|                                    |    | =====   |

13

Pushing the Possibilities

[BRADY WARE LOGO]

INDEPENDENT AUDITORS' REPORT ON CONSOLIDATED  
 SUPPLEMENTARY INFORMATION

-----

One South Main Street  
 Suite 600  
 Dayton, Ohio 45402  
 (937) 223-5247  
 (800) 893-4283  
 Fax (937) 223-0300

Board of Directors  
 QUALIA COMPUTING, INC. AND SUBSIDIARIES  
 Beavercreek, Ohio

One Woodside Drive  
 Richmond, Indiana 47374  
 (765) 966-0531  
 (800) 515-5536  
 Fax (765) 962-5015

www.bradyware.com

Our report on our audit of the basic financial statements of Qualia Computing, Inc. and Subsidiaries as of December 31, 2003 appears on page one. Our audit was conducted for the purpose of forming an opinion on the basic financial statements taken as a whole. The supplementary information (shown on page 15) is presented for purposes of additional analysis and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion is fairly stated in all material respects in relation to the basic financial statements taken as a whole for the nine months ended December 31, 2003.

/s/ BRADY WARE & SCHOENFELD, INC.

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Dayton, Ohio  
 February 3, 2004

## QUALIA COMPUTING, INC. AND SUBSIDIARIES

## CONSOLIDATED SCHEDULE OF SELLING, GENERAL AND ADMINISTRATIVE EXPENSES

-----  
NINE MONTHS ENDED DECEMBER 31, 2003

|                                     |               |
|-------------------------------------|---------------|
| Wages                               | \$ 4,691,594  |
| Bonuses                             | 429,516       |
| Payroll taxes                       | 236,371       |
| Employee benefits                   | 426,653       |
| 401(k) match and profit sharing     | 91,673        |
| Bank charges                        | 11,796        |
| Computer supplies                   | 32,853        |
| Repair and maintenance              | 28,341        |
| Consulting fees                     | 350,225       |
| Legal and professional fees         | 1,192,851     |
| Meals and entertainment             | 178,915       |
| Contributions                       | 11,399        |
| Travel                              | 831,844       |
| Training and seminars               | 4,691         |
| Office expense                      | 59,141        |
| Postage and freight                 | 215,849       |
| Rent and lease expense              | 382,161       |
| Market research                     | 73,160        |
| Dues and subscriptions              | 23,601        |
| Advertising                         | 779,398       |
| Depreciation expense                | 294,492       |
| Amortization expense                | 15,229        |
| Insurance                           | 131,504       |
| Miscellaneous taxes                 | 73,864        |
| Telephone and utilities             | 174,839       |
| Personal property taxes             | 16,660        |
| Licenses                            | 32,302        |
| Tuition assistance                  | 4,898         |
| Bad Debt                            | 332,957       |
| Relocation expense                  | 30,346        |
| Expenses allocated to cost of sales | (344,951)     |
|                                     | -----         |
|                                     | \$ 10,813,972 |
|                                     | -----         |

See independent auditors' report on consolidated supplementary information. 15



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### UNAUDITED PRO FORMA COMBINED CONDENSED FINANCIAL STATEMENTS

The following unaudited pro forma combined condensed financial statements give effect to the merger of iCAD, Inc. ("iCAD") and Qualia Computing, Inc. ("Qualia") using the purchase method of accounting, as required by Statement of Financial Accounting Standard No. 141, "Business Combinations." Under this method of accounting, iCAD allocated the purchase price to the fair value of assets acquired, including identified intangible assets and goodwill based on estimates it believes to be reasonable. The purchase price allocation is subject to revision when iCAD obtains additional information regarding asset valuation. The unaudited pro forma combined condensed balance sheet assumes the merger took place on September 30, 2003 and reflects the net proceeds of approximately \$5,900,000 from iCAD's November 2003 private placement of 1,260,000 shares of its common stock and additional investment rights which gave the investors in the offering the right to purchase, for a limited period, up to 315,000 additional shares of common stock at \$5.00 per share. The unaudited pro forma combined condensed statements of operations assume that the merger took place as of January 1, 2002. The unaudited pro forma information is presented for illustration purposes only in accordance with the assumptions set forth below. This information is not necessarily indicative of the operating results or of the financial position that would have occurred if the merger had been consummated on the dates indicated nor is it necessarily indicative of future operating results or financial position of the combined enterprise. The unaudited pro forma combined condensed financial information does not reflect any adjustments to reflect any cost savings or other synergies anticipated as a result of the merger.

|  | UNAUDITED PRO FORMA COMBINED CONDENSED BALANCE SHEET<br>AS OF SEPTEMBER 30, 2003 |            |                         |
|--|--|------------|-------------------------|
|  | iCAD (1)   | Qualia (2) | Proforma<br>Adjustments |
|  | -----  | -----      | -----                   |
| <b>Current assets:</b>   |  |            |                         |
| Cash and equivalents   | \$ 587,879   | \$ 446,031 | \$ (1,550,000)          |
|  |  |            | 5,900,000               |
| Trade accounts receivable, net of allowance<br>for doubtful accounts | 1,027,266  | 2,479,089  | (225,883)               |
| Inventory  | 531,402  | 1,457,636  |                         |
| Prepaid and other  | 177,713  | 63,523     |                         |
|  | -----  | -----      | -----                   |
| Total current assets   | 2,324,260  | 4,446,279  | 4,124,117               |
|  | -----  | -----      | -----                   |
| <b>Property and equipment:</b>                                       |  |            |                         |
| Equipment  | 953,722  | 1,581,794  |                         |
| Leasehold improvements   | 21,250   | 9,729      |                         |
| Furniture and fixtures   | 35,569   | 201,074    |                         |
|  | -----  | -----      | -----                   |
|  | 1,010,541  | 1,792,597  | -                       |
|  | -----  | -----      | -----                   |
| Less accumulated depreciation and amortization                       | 666,583  | 942,356    | -                       |
|  | -----  | -----      | -----                   |

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|                                |               |              |               |
|--------------------------------|---------------|--------------|---------------|
| Net property and equipment     | 343,958       | 850,241      | -             |
|                                | -----         | -----        | -----         |
| Other assets:                  |               |              |               |
| Identifiable intangible assets | 3,387,125     | 289,178      | 3,404,822     |
| Goodwill                       | 17,415,723    | -            | 25,789,497    |
| Other assets                   | -             | 345,414      |               |
| Patents, net                   | 94,643        |              |               |
|                                | -----         | -----        | -----         |
| Total other assets             | 20,897,491    | 634,592      | 29,194,319    |
|                                | -----         | -----        | -----         |
| Total assets                   | \$ 23,565,709 | \$ 5,931,112 | \$ 33,318,436 |
|                                | =====         | =====        | =====         |

PF1

|  |              |              |               |
|--|--------------|--------------|---------------|
| Current liabilities:                       |              |              |               |
| Accounts payable                           | \$ 1,765,368 | \$ 2,722,133 | (225,883)     |
| Accrued interest                           | 262,834      |              |               |
| Accrued expenses                           | 1,309,821    | 1,156,678    | 686,620       |
| Loans payable to sellers                   | -            |              |               |
| Note Payable                               | -            |              |               |
| Convertible subordinated debentures        | 10,000       | -            |               |
| Current maturities of note payable         | 69,048       | -            | 1,125,000     |
|  | -----        | -----        | -----         |
| Total current liabilities                  | 3,417,071    | 3,878,811    | 1,585,737     |
|  |              |              |               |
| Convertible promissory notes payable       | 2,930,000    | -            |               |
| Note payable, less current maturities      | 56,155       | -            | 3,375,000     |
|  | -----        | -----        | -----         |
| Total liabilities                          | 6,403,226    | 3,878,811    | 4,960,737     |
|  | -----        | -----        | -----         |
| Stockholders' equity:                      |              |              |               |
| Convertible preferred stock                | 86           | -            |               |
| Common stock                               | 273,978      | 17           | (17)          |
|  |              |              | 43,000        |
|  |              |              | 12,600        |
| Additional paid-in-capital                 | 88,130,846   | 36,488,492   | (36,488,492)  |
|  |              |              | 24,467,000    |
|  |              |              | 5,887,400     |
| Accumulated deficit                        | (70,292,163) | (34,531,251) | 34,531,251    |
| Cumulative translation adjustment          |              | 95,043       | (95,043)      |
| Treasury stock, at cost                    | (950,264)    |              |               |
|  | -----        | -----        | -----         |
| Stockholders' equity                       | 17,162,483   | 2,052,301    | 28,357,699    |
|  | -----        | -----        | -----         |
| Total liabilities and stockholders' equity | \$23,565,709 | \$ 5,931,112 | \$ 33,318,436 |
|  | =====        | =====        | =====         |

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- (1) The iCAD balance sheet is as of September 30, 2003.  
 (2) The Qualia balance sheet is as of December 31, 2003.

PF2

UNAUDITED PRO FORMA COMBINED CONDENSED STATEMENT OF OPERATIONS  
 FOR THE YEAR ENDED DECEMBER 31, 2002

|  | ICAD (1)     | Qualia (2)   | Proforma<br>Adjustments |
|--|--------------|--------------|-------------------------|
|  | -----        | -----        | -----                   |
| Sales                                    | \$ 6,246,432 | \$ 9,889,027 | \$ (23,309)             |
| Government grant revenue                 | -            | 101,847      |                         |
| Total revenues                           | 6,246,432    | 9,990,874    | (23,309)                |
| Cost of sales                            | 5,585,384    | 4,604,632    | (11,188)                |
| Gross margin                             | 661,048      | 5,386,242    | (12,121)                |
| Operating expenses:                      |              |              |                         |
| Engineering and product development      | 1,950,171    | 5,186,105    |                         |
| General and administrative               | 7,715,085    | 3,454,961    | 616,000                 |
| Marketing and sales                      | 987,587      | 9,535,139    |                         |
| Total operating expenses                 | 10,652,843   | 18,176,205   | 616,000                 |
| Loss from operations                     | (9,991,795)  | (12,789,963) | (628,121)               |
| Interest and other income (expense), net | (48,167)     | 215,772      | (246,094)               |
| Net loss before taxes                    | (10,039,962) | (12,574,191) | (874,215)               |
| Income tax provision (expense)           | -            | (8,766,361)  | 8,766,361               |
| Net loss                                 | (10,039,962) | (21,340,552) | 7,892,146               |
| Preferred dividends                      | 148,050      | -            |                         |

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|  |                 |                 |              |
|--|-----------------|-----------------|--------------|
| Net income (loss) available to common shareholders                     | \$ (10,188,012) | \$ (21,340,552) | \$ 7,892,146 |
| Net loss per share basic and diluted                                   | \$ (0.39)       |                 |              |
| Weighted average number of shares used in computing earnings per share | 26,000,177      |                 | 4,300,000    |

- (1) The iCAD financial statements for the year ended December 31, 2002 include the results of iCAD for the twelve months ended December 31, 2002 as adjusted to include twelve months results of ISSI which was acquired on June, 2002 (See Note 3).
- (2) The Qualia financial statements for the year ended December 31, 2002 include the results of Qualia for the 12 months ended March 31, 2003, the Company's fiscal year-end as adjusted to include the twelve-months results of CADx which was acquired on September 26, 2002. (See Note 4).

PF3

UNAUDITED PRO FORMA COMBINED CONDENSED STATEMENT OF OPERATIONS  
FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2003

|                                     | iCAD         | Qualia        | Pro Forma<br>Adjustments |
|-------------------------------------|--------------|---------------|--------------------------|
| Sales                               | \$ 4,938,629 | \$ 10,325,256 | \$ (237,789)             |
| Total revenues                      | 4,938,629    | 10,325,256    | (237,789)                |
| Cost of sales                       | 2,233,775    | 4,990,485     | (114,139)                |
| Gross margin                        | 2,704,854    | 5,334,771     | (123,650)                |
| Operating expenses:                 |              |               |                          |
| Engineering and product development | 1,813,560    | 2,727,329     |                          |
| General and administrative          | 6,370,414    | 2,682,668     | 462,000                  |
| Marketing and sales                 | 1,077,189    | 5,403,975     |                          |
| Total operating expenses            | 9,261,163    | 10,813,972    | 462,000                  |

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|  |                |                |              |
|--|----------------|----------------|--------------|
| Loss from operations   | (6,556,309)    | (5,479,201)    | (585,650)    |
|  | -----          | -----          | -----        |
| Interest and other (income) expense, net                               | 47,644         | 234,724        | 184,571      |
|  | -----          | -----          | -----        |
| Net loss   | (6,603,953)    | (5,713,925)    | (770,221)    |
| Preferred dividends  | 110,733        | -              |              |
|  | -----          | -----          | -----        |
| Net loss available to common shareholders                              | \$ (6,714,686) | \$ (5,713,925) | \$ (770,221) |
|  | =====          | =====          | =====        |
| Net loss per share basic and diluted                                   | \$ (0.25)      |                |              |
| Weighted average number of shares used in computing earnings per share | 26,531,177     |                | 4,300,000    |

PF4

NOTES TO UNAUDITED PRO FORMA COMBINED CONDENSED FINANCIAL STATEMENTS

1. BASIS OF PRO FORMA PRESENTATION

The unaudited pro forma combined condensed financial statements of iCAD have been prepared on the basis of assumptions relating to the allocation of consideration paid to the acquired assets and liabilities of Qualia based on management's best preliminary estimates. The actual allocation of the amount of the consideration may differ from that reflected in these unaudited pro forma combined condensed financial statements after a third party valuation and other procedures have been completed.

Below are tables of the estimated acquisition costs and estimated purchase price allocation for Qualia:

|  |              |
|--|--------------|
| Fair value of iCAD common stock issued                 | \$24,510,000 |
| Cash consideration and promissory note                 | 6,050,000    |
| Direct acquisition costs                               | 686,620      |
|  | -----        |
| Total purchase price                                   | \$31,246,620 |
|  | =====        |
| Net tangible assets acquired                           | \$ 1,763,123 |
| Estimated fair value of identifiable intangible assets | 3,694,000    |
| Goodwill   | 25,789,497   |
|  | -----        |
| Total Acquisition Cost                                 | \$31,246,620 |
|  | =====        |

2. PRO FORMA ADJUSTMENTS

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(a) Reflects the components of the purchase consideration and related transaction costs which consist of iCAD common stock with a market value of \$24,510,000, \$1,550,000 cash and a \$4,500,000 promissory note and direct acquisition costs of \$686,620. The value of iCAD common stock was based upon a per share value of \$5.70, equal to the closing price on November 28, 2003, the day the acquisition was announced. Also reflects the net proceeds of approximately \$5,900,000 for iCAD's November 2003 private placement of 1,260,000 shares of its common stock and additional investment rights to purchase up to 315,000 additional shares of common stock.

(b) Represents adjustments to increase the carrying values of identifiable intangible assets and record goodwill acquired.

(c) Reflects the elimination of amounts owed between iCAD and Qualia.

(d) Reflects the elimination of existing stockholders' equity of Qualia.

(e) Reflects the elimination of sales between iCAD and Qualia.

(f) Represents amortization of increase in value of acquired identifiable intangible assets of Qualia based upon average estimated useful lives of six years ( $3,694,000/6 \text{ years} = \$616,000 \text{ per year}$ )

(g) Reflects the increase in weighted average basic and diluted shares outstanding for the common stock issued in connection with the merger. Pro forma basic and diluted loss per share was calculated assuming that the 4,300,000 shares of iCAD common stock issued in connection with the merger were issued at the beginning of the period presented.

(h) Reflects the interest associated with the note payable of \$4,500,000 issued in connection with the Acquisition at an assumed expected average interest of 6.25%. Year ended December 31, 2002 - Average Borrowings of \$3,937,500 x 6.25% = \$246,094.

(i) Elimination of Qualia tax provision due to loss of combined entities.

PF5

### 3. ADJUSTMENTS TO ICAD FINANCIAL STATEMENTS

#### PRO FORMA FINANCIAL STATEMENT ICAD FOR THE YEAR ENDED DECEMBER 31, 2002

|                | iCAD         | ISSI         | Proforma<br>Adjustments |
|----------------|--------------|--------------|-------------------------|
|                | -----        | -----        | -----                   |
| Sales          | \$ 5,000,184 | \$ 1,602,452 | \$ (356,204)            |
| Total revenues | 5,000,184    | 1,602,452    | (356,204)               |
| Cost of sales  | 5,161,643    | 603,156      | (179,415)               |
|                | -----        | -----        | -----                   |

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|   |                |              |              |
|---|----------------|--------------|--------------|
| Gross margin  | (161,459)      | 999,296      | (176,789)    |
| Operating expenses:   |                |              |              |
| Engineering and product development                                       | 1,626,001      | 324,170      |              |
| General and administrative  | 6,595,076      | 938,509      | 181,500      |
| Marketing and sales   | 987,587        | -            |              |
| Total operating expenses  | 9,208,664      | 1,262,679    | 181,500      |
| Loss from operations  | (9,370,123)    | (263,383)    | (358,289)    |
| Interest and other income (expense),net                                   | (48,167)       | -            |              |
| Net income (loss) before tax  | (9,418,290)    | (263,383)    | (358,289)    |
| Income tax provision (expense)  | -              | -            |              |
| Net loss  | (9,418,290)    | (263,383)    | (358,289)    |
| Preferred dividends   | 148,050        | -            |              |
| Net income (loss) available<br>to common shareholders                     | \$ (9,566,340) | \$ (263,383) | \$ (358,289) |
| Net loss per share basic and diluted                                      | \$ (0.46)      |              |              |
| Weighted average number of shares used in<br>computing earnings per share | 20,928,397     |              | 5,071,780    |

Pro Forma Adjustments

(3a) Reflects the elimination of sales between iCAD and ISSI.

(3b) Reflects the amortization of intangible asset.

PF6

4. ADJUSTMENTS TO QUALIA FINANCIAL STATEMENTS

PRO FORMA FINANCIAL STATEMENT QUALIA  
FOR THE YEAR ENDED DECEMBER 31, 2002

|                          | Qualia    | CADx         | Proforma<br>Adjustments |
|--------------------------|-----------|--------------|-------------------------|
|                          | -----     | -----        | -----                   |
| Sales                    | 4,990,493 | \$ 5,196,534 | \$ (298,000)            |
| Government grant revenue | 101,847   | -            |                         |

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|   |              |                |           |
|---|--------------|----------------|-----------|
| Total revenues  | 5,092,340    | 5,196,534      | (298,000) |
| Cost of sales   | 2,216,179    | 2,388,453      |           |
| Gross margin  | 2,876,161    | 2,808,081      | (298,000) |
| Operating expenses:   |              |                |           |
| Engineering and product development                                       | 2,478,993    | 2,707,112      |           |
| General and administrative  | 2,438,235    | 1,016,726      |           |
| Marketing and sales   | 4,911,917    | 4,921,222      | (298,000) |
| Total operating expenses  | 9,829,145    | 8,645,060      | (298,000) |
| Loss from operations  | (6,952,984)  | (5,836,979)    | -         |
| Interest and other income (expense), net                                  | 215,772      | -              |           |
| Net loss before tax   | (6,737,212)  | (5,836,979)    | -         |
| Income tax provision (expense)  | (8,759,473)  | (6,888)        |           |
| Net loss  | (15,496,685) | (5,843,867)    | -         |
| Preferred dividends   | -            | -              |           |
| Net income (loss) available<br>to common shareholders                     | (15,496,685) | \$ (5,843,867) | \$ -      |
| Net loss per share basic and diluted                                      | \$ (10.61)   |                |           |
| Weighted average number of shares used in<br>computing earnings per share | 1,460,000    |                |           |

PRO FORMA ADJUSTMENTS

(4a) Reflects the elimination of Royalty between Qualia and CADx.

PF7

SIGNATURES

Pursuant to 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 hereunto duly authorized.

iCAD, INC.

By /s/ W. Scott Parr

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W. Scott Parr, President &  
Chief Executive Officer



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Dated: March 15, 2004