NANOBAC PHARMACEUTICALS INC
Form 10KSB/A
June 17, 2005

UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-KSB/A
Amendment to Annual Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For the fiscal year ended
December 31 2004

Nanobac Pharmaceuticals, Incorporated
(Exact name of registrant as specified in its charter)

Florida	**0-24696**	**59-3248917**
(State or Other Jurisdiction of Incorporation)	(Commission File Number)	(I.R.S. Employer Identification Number

2727 W. Dr. Martin Luther King Jr. Blvd, Suite 850, Tampa, Florida 33607
(Address of Principal Executive Office) (Zip Code)

(813) 264-2241
(Registrant's telephone number, including area code)

Securities registered under Section 12(b) of the Exchange Act: **None**

Securities registered under Section 12(g) of the Exchange Act:
Common Stock, without par value
(Title of Class)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for a shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes o No x

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-KSB/Aor any amendment to this Form 10-KSB/A. o

Indicate by check mark whether the Registrant is an accelerated filer (as defined in Rule 12b-2 of the Act): Yes o No x

State issuer's revenue for its most recent fiscal year: $358,361

The approximate aggregate market value of voting and non-voting stock held by non-affiliates of the registrant was $9,183,809 as of June 15, 2005. The shares of Common Stock held by each current executive officer and director and by each person who is known to the Company to own 5% or more of the outstanding Common Stock have been excluded from this computation on the basis that such persons may be deemed affiliates. The determination of affiliate status is not a conclusive determination for other purposes.

As of June 15, 2005 there were 187,340,093 shares of the Registrant's Common Stock outstanding.

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Nanobac Pharmaceuticals, Incorporated

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For the Year Ended December 31, 2004

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Amendment Number 1

In response to the Securities and Exchange Commission's periodic review of our filings under the Securities Exchange Act of 1934, the undersigned registrant hereby files Amendment No. 1 to amend the following Items with respect to its Annual Report on Form 10-KSB/A for the year ended December 31, 2004:

Item 7

We have amended Item 7, "Management Discussion and Analysis of Financial Condition and Results of Operations," to: (1) exclude non-GAAP information from the section titled “Selling, General and Administrative” and to revise the description to enhance the description of the components of this financial statement line item. And (2) to revise the section titled “Loss from continuing operations” to add a description for the following:

- the manner in which we use a non-GAAP measure to conduct or evaluate our business;
- the economic substance behind our decision to use such a measure;
- the material limitations associated with the use of the non-GAAP financial measure as compared to the use of the most directly comparable GAAP financial measure; and
- the substantive reasons why we believe the non-GAAP financial measure provides useful information.

Item 15

We have amended footnote 1 to our financial statements for the years ended December 31, 2004 and 2003 to correct the presentation of “Net loss per share”.

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PART II

Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations

During calendar 2004, and for the foreseeable future, our primary focus is on the research of the role Nanobacteria plays in human diseases in which pathologic calcification deposits are found. Since the beginning of 2004, there have been an increasing number of studies linking Nanobacteria to serious health problems, including cardiovascular diseases, peripheral vascular diseases, prostatitis, kidney stones, and Polycystic Kidney Disease. These studies have provided additional evidence of a relationship between Nanobacteria and these diseases in which pathological calcification is present. Our focus is in determining how Nanobacteria works and what countermeasures can be developed to better treat these diseases.

Recently we signed a collaborative agreement with the Mayo Foundation for Medical Education and Research to conduct research relating to the prevalence and treatment of nanobacteria in specific disease populations. The parties will evaluate the role of nanobacteria through four studies utilizing diagnostic test kits developed by Nanobac.

We continue with our collaborative efforts with scientists at NASA researching the effects of Nanobacteria in the formation of kidney stones under conditions simulating space flight. We also signed a collaborative agreement with Iowa State University to work with the Department of Geological and Atmospheric Sciences to explore novel methodologies for detecting calcified nano-particles which may be related to nanobacteria.

While there remains significant work ahead, we are encouraged by the progress being made in the study of Nanobacteria and the increasing level of acceptance in the medical community that there may be a relationship between the nano-particles we call Nanobacteria and the progression of certain diseases involving pathologic calcification. Our continuing research and development efforts, along with our efforts in obtaining recognition by various regulatory agencies (e.g. the FDA and similar agencies throughout the world), will require significant additional amounts of financing over the next several years.

We are attempting to protect the intellectual property rights to our discoveries including our treatment therapies and our diagnostic methods by obtaining patents. We currently have one issued patent and multiple patent applications for treatment therapies including the combination of EDTA and tetracycline to treat nanobacteria infections and the formula mix and treatment regimen for Nanobac Supplements, We also have one issued patent and multiple patent applications related to our diagnostic products We are attempting to further protect our intellectual property rights by obtaining additional patents in unique areas of research with respect to the role of Nanobacteria in pathologic calcification. These efforts are ongoing and will require significant additional infusions of financing to complete. It is also anticipated that additional patents will be sought in the future as our research and development efforts yield new discoveries.

We began direct sales of our Nanobac Supplements in June 2004. Nanobac Supplements are currently being marketed to the alternative medicine market and directly to the customer over the Internet. We anticipate that the Nanobac Supplements are the first generation of treatment therapies that we will develop and that the portfolio of treatments will increase as a result of our continuing research into the effect of Nanobacteria in numerous diseases.

During calendar 2004, our two diagnostic tests have gained additional recognition for their ability to identify Nanobacteria. We plan to initiate marketing our diagnostic testing kits in Europe during the first half of 2005.

During April 2004, we announced a name change from Nanobac Pharmaceuticals, Incorporated to Nanobac Life Sciences, Inc. to become effective upon approval by the shareholders.

Results of Operation

The following table presents the percentage of period-over-period dollar change for the line selected items in our Consolidated Statements of Operations for the years ended December 31, 2004 and 2003. These comparisons of financial results are not necessarily indicative of future results.

	Year ended December		
	2004	2003	% Change
Revenue	$ 358,361	$ 482,815	-26%
Cost of revenue	100,470	333,122	-70%
Gross Profit	257,891	149,693	72%
Gross Profit percentage	72%	31%	
Selling, general and administrative	4,765,841	2,128,375	124%
Research and development	2,375,363	540,426	340%
Depreciation and amortization	717,070	181,103	296%
Operating loss	(7,600,383)	(2,700,211)	181%
Other income (Expense)	(217,127)	(60,922)	256%
Loss from continuing operations	(7,817,510)	(2,761,133)	183%
Discontinued Operations	(57,268)	(938,358)	-94%
Net loss	($7,874,778)	($3,699,491)	113%

2004 Compared to 2003

Revenue

Revenue for the years ended December 31, 2004 and 2003 is summarized as follows:

	2004	2003
Nanobac Supplements	$ 230,321	$ 0
License revenue	46,800	0
Nanobac TX	0	407,242
Diagnostic Products	81,240	75,573
	$ 358,361	$ 482,815

During December 2003, we voluntarily discontinued offering NanobacTX, which accounted for 84% of our revenue for the year ended December 31, 2003. Accordingly, our revenue for the first half of 2004 was significantly reduced from the level experienced in the last half of 2003. During February 2004, we licensed a new product to an affiliated third party. Effective June 2004, the above license agreement was cancelled and we initiated sales of this product directly to customers under the name of Nanobac Supplements. We are in the process of accelerating our research and developing new products for better patient acceptance.

Revenue for the last quarter of 2004 averaged approximately $45,000 per month. Revenue for the year ended December 31, 2003 represents seven months of sales subsequent to our acquisition of LABS in June 2003.

Cost of revenue

Cost of revenue consists of direct materials, testing services (for diagnostic products) and shipping. As a percentage of revenue, cost of revenue was 28% for the year ended December 31, 2004 compared to 69% for the year ended December 31, 2003. Cost of revenue for 2003 included $150,000 of fixed lab fees for our diagnostic products. Without this fee, our cost of revenue would have been approximately 38% as a percentage of revenue. This fixed lab fee was eliminated in October 2003 and replaced with a variable cost structure, which significantly decreased cost of revenue.

In addition, the lower cost of revenue in 2004 was due in part to the 2004 license revenue having no direct costs. During June 2004, this licensing agreement was terminated and we initiated sales of Nanobac Supplements directly to customers, which has resulted in higher revenue and cost of revenue.

2004 Compared to 2003 (continued)

Gross Profit

Gross profit as a percentage of revenue was 72%, for the year ended December 31, 2004 compared to 31% for the year ended December 31, 2003. The increase in gross profit percentage is attributable to the 2004 license revenue having no costs and the existence of $150,000 of fixed lab costs in 2003 which were not incurred in 2004. We anticipate gross profit as a percentage of revenue to be between 65% and 70% for 2005.

Selling, General and Administrative

Selling, general and administrative ("SG&A") expenses for the years ended December 31, 2004 and 2003 are summarized as follows:

	Year ended December	
	2004	2003
Charges for stock issuances	$ 2,562,750	$ 750,000
Other SG&A	2,203,091	1,378,375
Total SG&A	$ 4,765,841	$ 2,128,375

The charges for stock issuances relate to stock issued as part of the Plan of Reorganization as confirmed by the Bankruptcy Court. There will be no further charges for stock issuances related to this bankruptcy.

For 2004, 64% of the Other SG&A expenses are comprised of payroll, travel and professional fees. Expenses to operate as a public company (primarily professional fees and investor relations costs) comprise an additional 18% of the remaining SG&A expense. Other significant SG&A expenses include facility rental and insurance.

The increase in SG&A for the year ended December 31, 2004 over December 31, 2003 (net of charges for stock issuances) is primarily attributable to the timing of the acquisition of LABS in June 2003. Only seven months of SG&A for LABS is included in the above SG&A expenses for 2003 compared to twelve months of expenses in 2004.

SG&A expenses for HealthCentrics are included in "Discontinued Operations".

2004 Compared to 2003 (continued)

Research and Development

For the year ended December 31, 2004, approximately 65% of research and development ("R&D") expenses are for payroll and medical director fees and approximately 25% of R&D expenses are for research studies. Expenses for research studies fluctuate from year to year as these expenses are dependent on specific initiatives and funding sources. Remaining R&D expenses include patents, our Finland lab and travel.

R&D expenses for the year ended December 31, 2004 increased 340% compared to the year ended December 31, 2003. The increase in R&D for the year ended December 31, 2004 over December 31, 2003 is primarily attributable to the acquisitions of LABS and OY. LABS was acquired in June 2003 and OY was acquired in November 2003 and includes our laboratory in Koupio Finland. Accordingly, only seven months of R&D for LABS and one and one-half months of R&D for OY are included in the above expenses for the year ended December 31, 2003 compared to twelve months for 2004. This increase also reflects our emphasis on R&D subsequent to the June 2003 acquisition of LABS. Specific increases include increased payroll, initiation of research studies, expansion of our patents and $500,000 of signing bonuses with the execution of employment agreements for key scientific personnel.

R&D expenses for HealthCentrics are included in "Discontinued Operations". We intend to continue to our R&D investment in the coming year.

Depreciation and amortization

Approximately 95% of depreciation and amortization are related to the amortization of intangible assets acquired in the 2003 and 2004 acquisitions of LABS and OY.

Other income (Expense)

Other income for the years ended December 31, 2004 and 2003 is summarized as follows:

	2004	2003
Interest expense		
Stockholder loan	($237,957)	($23,703)
Other	(10,096)	(19,231)
Foreign currency exchange gain	32,021	0
Other, net	(1,095)	(17,988)
	($217,127)	($60,922)

Foreign currency gain results from exchange rate changes between the U.S. dollar and the Euro on intercompany advances between our U.S. subsidiary and our Finland subsidiary.

2004 Compared to 2003 (continued)

Loss from continuing operations

Loss from continuing operations for the year ended December 31, 2004 was $7.8 million compared to $2.8 million for the year ended December 31, 2003. Excluding non-cash items for stock issuances and amortization and depreciation, the loss from continuing operations for the years ended December 31, 2004 and 2003 were as follows:

	2004	2003	Change
Loss from continuing operations	($7,817,510)	($2,761,133)	($5,056,377)
Depreciation and amortization	717,070	181,103	535,967
Charges for stock issuances	2,562,750	750,000	1,812,750
Loss from continuing operations excluding non-cash items	($4,537,690)	($1,830,030)	($2,707,660)

The loss from continuing operations excluding the above non-cash items increased $2.7 million for the year ended December 31, 2004 compared to the year ended December 31, 2003. This increase reflects $1.8 million of additional R&D costs and an additional five months of LABS SG&A expenses in 2004 compared to 2003.

The loss from continuing operations excluding non-cash items is a non-GAAP (Generally Accepted Accounting Principles) financial measure. We believe this measure is relevant for our company as this loss more closely approximates the amount of cash losses we are experiencing for the above periods. Non-GAAP financial measures have inherent, material limitations as compared to the use of GAAP financial measures. Non-GAAP financial measures are not defined within GAAP used in the United States and accordingly the calculation of non-GAAP financial measures can be interpreted differently by different sources. In addition, non-GAAP financial measures are not comparable to other public company operating results.

We are experiencing significant losses as we conduct research and development related to nanobacteria and launch our products and services. We believe it will take significant time before we will earn meaningful revenue to offset our expenses and there is no assurance that we will be able to accomplish this goal. As a result of the losses, we are dependent on affiliates of our CEO and other investors to provide sufficient cash sources to fund our operations.

2004 Compared to 2003 (continued)

Discontinued Operations

During October 2003, we decided to divest our HealthCentrics' business unit to focus exclusively on our nanobacteria business unit. We were unsuccessful in finding a buyer in 2003 for this business unit. During March 2004, this business unit was sold to an affiliate of our CEO for consideration of $250,000 plus assumption of net liabilities of approximately $499,000. Our gain on disposal of approximately $749,000 is accounted for as a capital contribution given the related party nature of the arrangement.

As a result of our decision to dispose of the HealthCentrics business unit, the operations of HealthCentrics were retroactively removed from continuing operations and disclosed as a single line item on the statements of operations. The loss from discontinued operations for the years ended December 31, 2004 and 2003 is summarized as follows:

	2004	2003
Revenue	$ 5,301	$ 19,970
Cost of revenue	9,208	62,570
Gross profit (loss)	(3,907)	(42,600)
Selling, general & administrative	53,361	692,407
Research and development	-	203,351
Net loss	($57,268)	($938,538)

Liquidity and Capital Resources

As of December 31, 2004, we had total assets of $9.7 million of which only $115,000 were current assets. At December 31, 2004, we had total current liabilities of $1.3 million and a working capital deficit of $1.2 million.

Since the United States Bankruptcy Court confirmed a plan of reorganization that allowed the Company to emerge from Chapter 11 during calendar 2002, the Company has financed its activities primarily through loans made by entities affiliated with our current Chief Executive Officer (referred to herein as “the Affiliated Entities”). These loans were made as funding was needed and were extremely advantageous to the Company in that the amounts were funded as the Company needed financial infusions and allowed the Company to avoid the costs and distractions of attempting to raise these amounts from unrelated parties. It is unrealistic to believe that unrelated parties would have offered terms as generous as those obtained from the Affiliated Entities, and it is also unlikely that any financing could have been obtained under any terms without the financing of the Affiliated Entities.

As discussed in Item 5, from time to time the Affiliated Entities have agreed to allow a portion of the loan balances to be converted into shares of the Company’s common stock. On September 30, 2004, $7,500,000 of the loan balance was converted into 29,999,964 shares of our common stock at a price of $.25 per share. There is no obligation on the part of the Affiliated Entities to make additional loans to the Company. The Affiliated Entities are also under no obligation to convert any portion of the loan balances owed to it into additional shares of the Company’s stock.

As is also discussed in Item 5, since August of 2004, the Company has received $1.4 million (net of $125,000 of expenses) from three unaffiliated investors and one affiliate for shares of the Company’s stock and an equal amount of warrants to acquire additional shares of the Company’s stock. The exact number of shares to be issued is dependent upon the average closing bid price of the Company’s stock on the five trading days immediately prior to the date on which a registration statement for these shares is declared effective. The purchase price of the shares is equal to the lesser of (1) $.12 or (2) 52% of the average closing price described above. An additional $1.5 million is to be received from these investors within five days of registering the common shares and warrants. A registration statement has not yet been filed for these shares. Successful registration of the shares contemplated under the agreements discussed above will provide significant amounts of needed capital into the Company. However, a registration statement has not yet been filed with the Securities and Exchange Commission (“SEC”) and there are no assurances that the SEC will declare a registration statement effective.

Net cash used in operations was $3.4 million for the year ended December 31, 2004. The negative cash flow from operations reflects the $7.9 million net loss for the year offset by the non-cash charge for common stock issuances of $2.6 million, depreciation and amortization of $717,000, interest expense added to the principal balance of the stockholder loan of $238,000, and an increase in current liabilities of approximately $1.0 million.

Liquidity and Capital Resources (continued)

Net cash provided by investing activities was approximately $165,000 for the year ended December 31, 2004, which reflects the receipt of $200,000 from a common stock option exercise related to the acquisition of LABS offset by our purchase of fixed assets of approximately $37,000.

Net cash provided by financing activities was $3.2 million for the year ended December 31, 2004, which is attributable to stockholder loans of $2.1 million and $1.2 million from common stock Subscription Agreements as described in the preceding paragraphs.

We are dependent on raising additional funding necessary to implement our business plan as outlined above. Should we not be successful in raising cash from the Affiliated Entities and other investors, we are unlikely to continue as a going concern.

Recent Accounting Pronouncements

In November 2004, the FASB issued SFAS No. 151, “Inventory Costs.” The statement amends Accounting Research Bulletin (“ARB”) No. 43, “Inventory Pricing,” to clarify the accounting for abnormal amounts of idle facility expense, freight, handling costs, and wasted material. ARB No. 43 previously stated that these costs must be “so abnormal as to require treatment as current-period charges.” SFAS No. 151 requires that those items be recognized as current-period charges regardless of whether they meet the criterion of “so abnormal.” In addition, this statement requires that allocation of fixed production overhead to the costs of conversion be based on the normal capacity of the production facilities. The statement is effective for inventory costs incurred during fiscal years beginning after June 15, 2005, with earlier application permitted for fiscal years beginning after the issue date of the statement. The adoption of SFAS No. 151 is not expected to have any significant impact on our current financial condition or results of operations.

In December 2004, the FASB issued SFAS No. 153, “Exchanges of Nonmonetary Assets - An Amendment of APB Opinion No. 29.” APB Opinion No. 29, “Accounting for Nonmonetary Transactions,” is based on the opinion that exchanges of nonmonetary assets should be measured based on the fair value of the assets exchanged. SFAS No. 153 amends Opinion No. 29 to eliminate the exception for nonmonetary exchanges of similar productive assets and replaces it with a general exception for exchanges of nonmonetary assets whose results are not expected to significantly change the future cash flows of the entity. The adoption of SFAS No. 153 is not expected to have any impact on our current financial condition or results of operations.

Recent Accounting Pronouncements (continued)

In December 2004, the FASB revised its SFAS No. 123 ("SFAS No. 123R"), "Accounting for Stock Based Compensation." The revision establishes standards for the accounting of transactions in which an entity exchanges its equity instruments for goods or services, particularly transactions in which an entity obtains employee services in share-based payment transactions. The revised statement requires a public entity to measure the cost of employee services received in exchange for an award of equity instruments based on the grant-date fair value of the award. That cost is to be recognized over the period during which the employee is required to provide service in exchange for the award. Changes in fair value during the requisite service period are to be recognized as compensation cost over that period. In addition, the revised statement amends SFAS No. 95, "Statement of Cash Flows," to require that excess tax benefits be reported as a financing cash flow rather than as a reduction of taxes paid. The provisions of the revised statement are effective for financial statements issued for the first interim or annual reporting period beginning after June 15, 2005, with early adoption encouraged. We are currently evaluating the impact that this statement will have on our financial condition or results of operations.

Critical accounting policies

Use of estimates - The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Contractual obligations

At December 31, 2004, the Company's contractual cash obligations, with initial or remaining terms in excess of one year, were as follows:

	Amount of Commitment Expired by year ending December 31,		
	Other Liability	Operating Leases	Total
Less than 1 year	$ -	$ 174,281	$ 174,281
1 - 2 years	350,000	287,633	637,633
3 - 4 years	-	112,063	112,063
5 - 7 years	-	27,234	27,234
Total	$ 350,000	$ 601,211	$ 951,211

Forward Looking Statements

Our disclosure and analysis in this 2004 Form 10-KSB/A contains some forward-looking statements, within the meaning of the Private Securities Litigation Reform Act of 1995 (“the Act”), that set forth anticipated results based on our plans and assumptions. From time to time, we also provide forward-looking statements in other materials we release to the public as well as oral forward-looking statements. Such statements give our current expectations or forecasts of future events; they do not relate strictly to historical and current facts. We have tried wherever possible to identify such statements by using words such as “anticipate”, “estimate”, “expect”, “project”, “intend”, “plan”, “believe”, “will similar expressions in connection with any discussion of future operating or financial performance.

In light of the important factors that can materially affect results, including those set forth above and elsewhere in this report, the inclusion of forward-looking information herein should not be regarded as a representation by us or any other person that our objectives or plans will be achieved. We may encounter competitive, technological, financial and business challenges making it more difficult than expected to continue to market our products and services; competitive conditions within our industry may change adversely; we may be unable to retain existing key management personnel; our forecasts may not accurately anticipate market demand; and there may be other material adverse changes in our operations or business. Certain important factors affecting the forward looking statements made herein include, but are not limited to (i) accurately forecasting capital expenditures; (ii) obtaining new sources of external financing; (iii) serving as the nexus for nanobacteria research and (iv) conducting successful clinical trials supporting Dr. Kajander’s theories that the human body does not recognize nanobacteria as harmful, and accordingly, nanobacteria could be the cause of pathological disease causing calcification found in multiple diseases. Assumptions relating to budgeting, marketing, product development and other management decisions are subjective in many respects and thus susceptible to interpretations and periodic revisions based on actual experience and business developments, the impact of which may cause the Company to alter its capital expenditure or other budgets, which may in turn affect the Company's financial position and results of operations.

Risk Factors

Trends, Risks and Uncertainties

We have sought to identify what we believe to be the most significant risks to our business. However, we cannot predict whether, or to what extent, any of such risks may be realized nor can we guarantee that we have identified all possible risks that might arise. You should not consider the risks and assumptions identified in this report to be a complete discussion of all potential risks and uncertainties affecting the Company. Investors should carefully consider all risk factors before making an investment decision with respect to our Common Stock.

Cautionary Factors that may affect Future Results

We provide the following cautionary discussion of risks, uncertainties and possible inaccurate assumptions relevant to our business and our products. These are factors that we think could cause our actual results to differ materially from expected results. Other factors besides those listed here could adversely affect us.

Risk Factors (continued)

We require additional financing in order to continue in business as a going concern, the availability of which is uncertain. We may be forced by business and economic conditions to accept financing terms which will require us to issue our securities at a discount, which could result in further dilution to our existing stockholders.

As discussed under the heading, "Management's Discussion and Analysis - Liquidity and Capital Resources," we require additional financing to fund our operations. There can be no assurance that additional financing will be available to us when needed or, if available, that it can be obtained on commercially reasonable terms. In addition, any additional equity financing may involve substantial dilution to our stockholders. If we fail to raise sufficient financing to meet our immediate cash needs, we will be forced to scale down or perhaps even cease the operation of our business, which may result in the loss of some or all of your investment in our common stock.

In addition, in seeking debt or equity private placement financing, we may be forced by business and economic conditions to accept terms which will require us to issue our securities at a discount from the prevailing market price or face amount, which could result in further dilution to our existing stockholders.

Liquidity and Working Capital Risks; Need for Additional Capital to Finance Growth and Capital Requirements

Throughout 2004 and 2003, affiliates of our Chief Executive Officer have provided our capital needs through loans and capital contributions. While these affiliates continue to provide for the majority of our cash requirements, they are under no obligation to continue such financing and/or strategic guidance. In the event these affiliates should discontinue their support, we may have difficulty in continuing our operations. In such an event, shareholders could lose their investment in its entirety. Historically, these affiliates have provided capital to us on a demand debt basis after which they may convert debt into shares of our common stock. If, in the future we require additional capital, these affiliates may contribute some or all of our requirements. We anticipate that as a part of any such loan, these affiliates would have rights to convert into additional shares of our common stock. In such an event and to the degree of which we require these affiliates' support, shareholders may experience dilution. At present, we do not maintain key man insurance for our CEO.

In addition to the financial support we may receive from affiliates of our CEO, we may continue to seek to raise capital from public or private equity or debt sources to provide working capital to meet our general and administrative costs until net revenues make the business self-sustaining. We cannot guarantee that we will be able to raise any such capital on terms acceptable to us or at all. Such financing may be upon terms that are dilutive or potentially dilutive to our stockholders. If alternative sources of financing are required, but are insufficient or unavailable, we will be required to modify our growth and operating plans in accordance with the extent of available funding.

Risk Factors (continued)

We have a history of operating losses and fluctuating operating results, which raise substantial doubt about our ability to continue as a going concern.

Since inception through December 31, 2004, we have incurred aggregate losses of $13.0 million. Our net loss for the year ended December 31, 2004 and 2003 was $7.9 million and $3.7 million, respectively. There is no assurance that we will operate profitably or will generate positive cash flow in the future. In addition, our operating results in the future may be subject to significant fluctuations due to many factors not within our control, such as the unpredictability of when customers will order products, the size of customers' orders, the demand for our products, and the level of competition and general economic conditions.

Although we are confident that revenues will increase, we also expect an increase in research and development costs and operating costs. Consequently, we expect to incur operating losses and negative cash flow until our products gain market acceptance sufficient to generate a commercially viable and sustainable level of sales, and/or additional products are developed and commercially released and sales of such products made so that we are operating in a profitable manner.

Potential Incorrect Conclusions on the Detection and Eradication of Nanobacteria

Most of our future revenue is based on our ability to detect and eradicate Nanobacteria. If it is ultimately proved that our diagnostic methodologies and treatment regimens as covered by our patents are ineffective or based upon incorrect scientific conclusions, our existing patents and product lines may lose most or all of their value. Further, if we are unsuccessful in leveraging our diagnostic and therapeutic products to detect and treat nanobacterial diseases, we may not generate sufficient revenue to offset our expenses.

Acceptance of Products in the Marketplace is Uncertain.

Our future financial performance will depend, at least in part, upon the introduction and customer acceptance of our proposed treatments and products. Our treatments and products may not achieve market acceptance, and such adverse marketing results could materially harm the Company.

Risk Factors (continued)

Limited Operating History Anticipated Losses; Uncertainty of Future Results

We have a limited operating history upon which an evaluation of our Company and our prospects can be based. Our prospects must be evaluated with a view to the risks encountered by companies in early stages of development, particularly in light of the uncertainties relating to the new and evolving biolife science research which we intend to develop and market, and the acceptance of our business model. We will be incurring costs to: (i) perform research studies to prove the effectiveness of our pharmaceutical products, (ii) further develop and market our products; (iii) establish distribution relationships; and (iv) build an organization. To the extent that such expenses are not subsequently followed by commensurate revenues, our business, results of operations and financial condition will be materially adversely affected. We, therefore, cannot insure that we will be able to immediately generate sufficient revenues. We expect negative cash flow from operations to continue for at least the next 12 months as we continue to develop and market our business. If cash generated by operations is insufficient to satisfy our liquidity, we may be required to sell additional equity or debt securities. The sale of additional equity or convertible debt securities would result in additional dilution to our stockholders. Our initial operations may not be profitable, since time will be required to build our business to the point that our revenues will be sufficient to cover our total operating costs and expenses. Our reaching a sufficient level of sales revenues will depend upon a large number of factors, including availability of sufficient working capital, the number of customers we are able to attract and the costs of continuing development of our product line.

Federal Food and Drug Administration

Some or all of our products may be governed by rules and regulations established by the United States Food and Drug Administration (“FDA”). Changes in FDA regulations and the enforcement thereof may affect our biolife science business. Furthermore, we may not be successful in filing and obtaining approval of our 510K or PMA filings with the FDA for our Nano-Capture Antigen and Nano-Sero IgG ELISA assays.

Data Obtained Through Clinical Trials.

Data obtained from pre-clinical studies and clinical trials do not necessarily predict results that will be obtained from later pre-clinical studies and clinical trials. Moreover, pre-clinical and clinical data is susceptible to varying interpretations, which could delay, limit or prevent regulatory approval. A number of companies in the pharmaceutical industry have suffered significant setbacks in advanced clinical trials, even after experiencing promising results in earlier trials. The failure to adequately demonstrate the safety and/or effectiveness of an intended product under development could delay or prevent regulatory clearance of the potential drug or treatment, resulting in delays to commercialization, and could materially harm the business.

Risk Factors (continued)

Competitors in the Pharmaceutical Industry May Develop Competing Technologies

Drug companies and/or other health care companies may seek to develop and market technologies which may compete with our Company's technology. While we believe that our technology regarding the prescription treatment of nanobacterial infections caused by nanobacterium sanguineum is unique, other competitors may develop similar or different treatments which may become more accepted by the marketplace.

Regulations may Inhibit our Ability to Sell Nanobac Supplements

Codex is a joint body comprising government representatives and non-governmental organizations, jointly managed by the United Nation's (U.N.) Food and Agriculture Organization (FAO) and the World Health Organization (WHO) of the U.N. The Codex Committee on Nutrition and Foods for Special Dietary Uses (CCNFSDU) has been attempting to develop international guidelines for vitamins and minerals since 1991. In November 2004, these guidelines were finalized and a vote to ratify will take place in July, 2005.

There is a school of thought within the dietary supplement community that buying vitamins and other dietary supplements will be severely limited by this CODEX. Passage of the above guidelines may inhibit our ability to sell Nanobac Supplement outside of the United States. We do not believe that the passage will impact United State revenue as the U.S. draft position states that "The United States supports consumer choice and access to dietary supplements that are safe and are labelled in a truthful and non-misleading manner." Further, the CODEX Draft notes that the Codex Guidelines for Vitamin and Mineral Supplements will not adversely affect the availability of safe and truthfully labelled supplement products in the U.S. marketplace or to U.S. consumers. If our interpretation is not correct passage of the international guidelines may inhibit the sales of Nanobac Supplement inside and outside of the United States

Risk of Third Party Lawsuits.

We are exposed to potential product liability risks that are inherent in the testing, manufacturing and marketing of pharmaceutical products. We cannot assure potential investors that such claims will not be asserted against the Company. A successful liability claim or series of claims brought against us could have a material adverse effect on our financial condition. In addition, we may be sued by third parties who claim that our products and treatments infringe upon the intellectual property rights of others or that we have misappropriated trade secrets of others. This risk is exacerbated by the fact that the validity and breadth of claims covered in medical technology patents and the breadth and scope of trade secret protection involve complex legal and factual questions for which important legal principles are unresolved. Any litigation or claims against us, whether or not valid, could result in substantial costs, could place a significant strain on our financial resources, and could harm our reputation.

Risk Factors (continued)

Government Regulation

Healthcare in general and the pharmaceuticals industry in particular are highly regulated markets, subject to both federal and a multitude of state regulations and guidelines. The majority of our business is still in clinical research applications and is governed by the medical community. There can be no assurance that changes to state or federal laws will not materially restrict our ability to sell our products or develop new product lines.

Intellectual Property Rights

We have a family of patents encompassing the detection and eradication of nanobacteria. There are risks inherent in any intellectual property rights in that they may be challenged as being invalid or not original. Additionally, other parties may abuse such intellectual rights, causing the Company to defend its rights.

Dependency upon Key Technical and Scientific Personnel Who May Terminate Employment at Any Time.

Our success will depend to a significant degree upon the continued services of key technical and scientific personnel, including but not limited to E. Olavi Kajander, MD, PhD. In addition, our success may depend on our ability to attract and retain other highly skilled personnel. Competition for qualified personnel is intense, and the process of hiring and integrating such qualified personnel is often lengthy. We may be unable to recruit personnel on a timely basis, if at all. All of the Company's management and other employees may voluntarily terminate their employment with us at any time. The loss of the services of key personnel, or the inability to attract and retain additional qualified personnel, could result in delays to development, loss of sales, and/or diversion of management resources that could have a material adverse affect on the Company.

Competition

The markets in which we compete include successful and well-capitalized competitors that vary in size and scope. Principal competitors include Pfizer, Merck and other pharmaceutical companies having unique treatments for cardiovascular disease. All of these competitors are more established, benefit from greater name recognition and have substantially greater resources than us. Moreover, we could face additional competition as other established and emerging companies enter the market and new products and technologies are introduced. Increased competition could result in price reductions, fewer customer subscriptions, reduced gross margins and loss of market share, any of which could materially adversely affect our business, financial condition and operating results. In addition, current and potential competitors may make strategic acquisitions or establish cooperative relationships among themselves or with third-parties, thereby increasing the ability of their products to address the needs of our prospective consumers. While we believe we can differentiate our product from these current and future competitors, focusing on the products' functionality, flexibility, adaptability and features, there can be no assurance that we will be able to compete successfully against current and future competitors. The failure to effectively compete would have a material adverse effect upon our business, financial condition and operating results.

Risk Factors (continued)

Lack of Independent Directors

We cannot guarantee our Board of Directors will have a majority of independent directors in the future. In the absence of a majority of independent directors, our executive officers, who are also principal stockholders and directors, could establish policies and enter into transactions without independent review and approval thereof. This could present the potential for a conflict of interest between the Company's stockholders and the controlling officers and/or directors.

Limitation of Liability and Indemnification of Officers and Directors

Our officers and directors are required to exercise good faith and high integrity in our management affairs. Our Articles of Incorporation and By Laws provide, however, that our officers and directors shall have no liability to our shareholders for losses sustained or liabilities incurred which arise from any transaction in their respective managerial capacities unless they violated their duty of loyalty, did not act in good faith, engaged in intentional misconduct or knowingly violated the law, approved an improper dividend or stock repurchase, or derived an improper benefit from the transaction. Our Articles and By-Laws also provide for the indemnification by us of the officers and directors against any losses or liabilities they may incur as a result of the manner in which they operate our business or conduct the internal affairs, provided that in connection with these activities they act in good faith and in a manner they reasonably believe to be in, or not opposed to, the best interests of the Company, and their conduct does not constitute gross negligence, misconduct or breach of fiduciary obligations.

Continued Control by Current Officers and Directors

The present officers and directors control approximately 50% of the outstanding shares of Common Stock, and are in a position to elect all of our Directors and otherwise control the Company, including, without limitation, authorizing the sale of equity or debt securities of the Company, the appointment of officers, and the determination of officer's salaries. Shareholders have no cumulative voting rights.

Risk Factors (continued)

Limited Market Due To Penny Stock

The Company's stock differs from many stocks, in that it is a "penny stock." The Securities and Exchange Commission has adopted a number of rules to regulate penny stocks. These rules include, but are not limited to, Rules 3a5l-l, 15g-1, 15g-2, 15g-3, 15g-4, 15g-5, 15g-6 and 15g-7 under the Securities and Exchange Act of 1934, as amended. Because our securities probably constitute penny stock within the meaning of the rules, the rules would apply to us and our securities. The rules may further affect the ability of owners of our stock to sell their securities in any market that may develop for them. There may be a limited market for penny stocks, due to the regulatory burdens on broker-dealers. The market among dealers may not be active. Investors in penny stock often are unable to sell stock back to the dealer that sold them the stock. The mark-ups or commissions charged by the broker-dealers may be greater than any profit a seller may make. Because of large dealer spreads, investors may be unable to sell the stock immediately back to the dealer at the same price the dealer sold the stock to the investor. In some cases, the stock may fall quickly in value. Investors may be unable to reap any profit from any sale of the stock, if they can sell it at all. Stockholders should be aware that, according to the Securities and Exchange Commission Release No. 34- 29093, the market for penny stocks has suffered in recent years from patterns of fraud and abuse. These patterns include: - Control of the market for the security by one or a few broker-dealers that are often related to the promoter or issuer; - Manipulation of prices through prearranged matching of purchases and sales and false and misleading press releases; - "Boiler room" practices involving high pressure sales tactics and unrealistic price projections by inexperienced sales persons; - Excessive and undisclosed bid-ask differentials and markups by selling broker-dealers; and - The wholesale dumping of the same securities by promoters and broker- dealers after prices have been manipulated to a desired level, along with the inevitable collapse of those prices with consequent investor losses. Furthermore, the penny stock designation may adversely affect the development of any public market for the Company's shares of common stock or, if such a market develops, its continuation. Broker-dealers are required to personally determine whether an investment in penny stock is suitable for customers. Penny stocks are securities (i) with a price of less than five dollars per share; (ii) that are not traded on a "recognized" national exchange; (iii) whose prices are not quoted on the NASDAQ automated quotation system (NASDAQ-listed stocks must still meet requirement (i) above); or (iv) of an issuer with net tangible assets less than $2,000,000 (if the issuer has been in continuous operation for at least three years) or $5,000,000 (if in continuous operation for less than three years), or with average annual revenues of less than $6,000,000 for the last three years. Section 15(g) of the Exchange Act, and Rule 15g-2 of the Commission require broker-dealers dealing in penny stocks to provide potential investors with a document disclosing the risks of penny stocks and to obtain a manually signed and dated written receipt of the document before effecting any transaction in a penny stock for the investor's account. Potential investors in the Company's common stock are urged to obtain and read such disclosure carefully before purchasing any shares that are deemed to be "penny stock." Rule 15g-9 of the Commission requires broker-dealers in penny stocks to approve the account of any investor for transactions in such stocks before selling any penny stock to that investor. This procedure requires the broker-dealer to (i) obtain from the investor information concerning his or her financial situation, investment experience and investment objectives; (ii) reasonably determine, based on that information, that transactions in penny stocks are suitable for the investor and that the investor has sufficient knowledge and experience as to be reasonably capable of evaluating the risks of penny stock transactions; (iii) provide the investor with a written statement setting forth the basis on which the broker-dealer made the determination in (ii) above; and (iv) receive a signed and dated copy of such statement from the investor, confirming that it accurately reflects the investor's financial situation, investment experience and investment objectives. Compliance with these requirements may make it more difficult for the Company's stockholders to resell their shares to third parties or to otherwise dispose of them.

PART IV

Item 15. Exhibits, Financial Statement Schedules and Reports on Form 8-K

(a) The following documents are filed as part of this report:

(1) Financial Statements

The following Financial Statements are included herein:

	Page Number
Ÿ Report of Aidman Piser & Company, Independent Auditors	F-1
ŸConsolidated Balance Sheet at December 31, 2004	F-2
ŸConsolidated Statements of Operations for the years ended December 31, 2004 and 2003	F-3
ŸConsolidated Statements of Stockholders' Equity (Deficit) for the years ended December 31, 2004 and 2003	F-4
ŸConsolidated Statements of Cash Flows for the years ended December 31, 2004 and 2003	F-5
ŸNotes to Consolidated Financial Statements	F-6-F-22

(2) Financial Statement Schedules

Financial Statement Schedules have been omitted because they are not applicable or are not required or the information required to be set forth therein is included in the consolidated financial statements or notes thereto.

EXHIBIT INDEX

Exhibit Number	Description
23.1	Consent of Aidman, Piser & Company, P.A.
31.1	Certification to Section 302 of the Sarbanes-Oxley Act of 2002 - Chief Executive Officer
31.2	Certification to Section 302 of the Sarbanes-Oxley Act of 2002 - Chief Financial Officer
32.1	Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 - Chief Executive Officer
32.2	Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 - Chief Financial Officer

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned; thereunto duly authorized, on this 16th day of June, 2005.

Nanobac Pharmaceuticals, Incorporated

By: /s/ John D. Stanton

John D. Stanton
Chief Executive Officer

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of Registrant and in the capacities indicated on June 16, 2005.

Signature	**Title**
/s/ John D. Stanton John D. Stanton	Chairman of the Board of Directors Chief Executive Officer and Chief Financial Officer (Principal Executive and Financial Officer)
/s/ Alexander Edwards III Alexander Edwards III	Director
/s/ Jan Egberts Jan Egberts, M.D.	Director
/s/ Stephan Rechtschaffen Stephan Rechtschaffen, M.D.	Director
/s/ Michael J Dean Michael J Dean	Vice President - Finance and Controller (Principal Accounting Officer)

Independent Auditors' Report

Board of Directors
Nanobac Pharmaceuticals, Incorporated and Subsidiaries
Tampa, Florida

We have audited the accompanying consolidated balance sheet of Nanobac Pharmaceuticals, Incorporated and Subsidiaries (F/K/A American Enterprise Corporation) (the "Company"), as of December 31, 2004, and the related consolidated statements of operations, stockholders' deficit and cash flows for the two years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audit in accordance with standards of the Public Accounting Oversight Board (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. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. Our audit included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit 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 audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Nanobac Pharmaceuticals, Incorporated and Subsidiaries, at December 31, 2004, and the consolidated results of their operations and their cash flows for the two years then ended in conformity with accounting principles generally accepted in the United States of America.

The accompanying financial statements have been prepared assuming that the Company will continue as a going concern. As discussed in Note 1 to the financial statements, the Company has suffered recurring losses from operations, has working capital and net capital deficiencies and is dependent upon continued financing from stockholders and outside investors, all of which raise substantial doubt about its ability to continue as a going concern. Management's plans in regard to these matters are also described in Note 1. The financial statements do not include any adjustments that might result from the outcome of this uncertainty.

/s/ Aidman, Piser & Company, P.A.

April 12, 2005, except for Note 1, for which
the date is June 10, 2005
Tampa, Florida

NANOBAC PHARMACEUTICALS INCORPORATED AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEET

		December 31, 2004
ASSETS		
CURRENT ASSETS		
Cash	$	17,908
Account receivable		3,395
Inventory		70,571
Prepaid expenses		23,649
Total current assets		115,523
FIXED ASSETS, less accumulated depreciation of $84,143		124,995
OTHER ASSETS		
Security deposits		68,054
Intangible assets, less accumulated amortization of $832,701		5,760,342
Goodwill		3,615,393
Total other assets		9,443,789
TOTAL ASSETS	$	9,684,307
LIABILITIES AND STOCKHOLDERS' EQUITY		
CURRENT LIABILITIES		
Accounts payable	$	645,491
Accrued compensation		50,611
Accrued expenses		335,861
Short-term note payable		62,379
Other liabilities		16,423
Stockholder loans		194,068
Total current liabilities		1,304,833
LONG-TERM LIABILITIES		
Accrued compensation		350,000
Stock settlement liability		1,918,630
Total liabilities		3,573,463
COMMITMENTS AND CONTINGENCY (Notes 9, 11 and 13)		-
STOCKHOLDERS' EQUITY		
Common stock, no par value, 250,000,000 shares authorized, 187,240,093 shares issued and outstanding		16,296,550
Preferred stock, no par value, 1,000,000 shares authorized, no shares issued and outstanding		-
Additional paid-in capital		3,539,328
Accumulated deficit		(13,049,568)
Accumulated other comprehensive loss		(675,466)

Total stockholders' equity		6,110,844
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	$	9,684,307

The accompanying notes are an integral part of these financial statements

NANOBAC PHARMACEUTICALS INCORPORATED AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF OPERATIONS

	Year ended December 31, 2004	Year ended December 31, 2003
REVENUE	$ 358,361	$ 482,815
COST OF REVENUE	100,470	333,122
GROSS PROFIT	257,891	149,693
OPERATING EXPENSES		
Sales, general and administrative	4,765,841	2,128,375
Research and development	2,375,363	540,426
Depreciation and amortization	717,070	181,103
Total Operating Expenses	7,858,274	2,849,904
OPERATING LOSS	(7,600,383)	(2,700,211)
OTHER INCOME (EXPENSES)		
Interest expense	(248,053)	(42,934)
Foreign currency exchange gain	32,021	-
Other, net	(1,095)	(17,988)
LOSS FROM CONTINUING OPERATIONS BEFORE INCOME TAXES	(7,817,510)	(2,761,133)
PROVISION FOR INCOME TAXES	-	-
LOSS FROM CONTINUING OPERATIONS	(7,817,510)	(2,761,133)
DISCONTINUED OPERATIONS:		
Loss from discontinued operations (no applicable income taxes)	(57,268)	(938,358)
NET LOSS	$ (7,874,778)	$ (3,699,491)
LOSS PER COMMON SHARE (BASIC AND DILUTED):		
Continuing operations	$ (0.05)	$ (0.04)
Discontinued operations	0.00	(0.01)
Net loss	$ (0.05)	$ (0.05)
WEIGHTED AVERAGE NUMBER OF		

COMMON SHARES OUTSTANDING		
Basic and Diluted	152,903,084	67,489,524

The accompanying notes are an integral part of these financial statements

NANOBAC PHARMACEUTICALS INCORPORATED AND SUBSIDIARIES
CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY (DEFICIT)
FOR THE YEARS ENDED DECEMBER 31, 2003 AND 2004

	Common Shares	Stock Value	Preferred Shares	Stock Value	Additional Paid-in Capital	Due from Option Exercise	Accumulated Deficit	Oth Compre Lo
December 31, 2002 Balance	19,982,965	$ 1,134,377	368,815	$ -	$ -	$ -	($1,475,299)	$
Conversion of preferred stock to common stock	16,268,430	-	(368,815)	-	-	-		
Stock issued in connection with bankruptcy	23,335,445	399,516	794,569	350,484	-	-	-	
Stock issues for services	50,000	30,175	-	-	-	-	-	
Conversion of liabilities to shares of common stock	3,644,000	728,800	-	-	-	-	-	
Sale of common stock (see Notes 1 and 10)	1,690,000	548,000	-	-	-	-	-	
Common stock issued in acquisition of NanobacLabs Pharmaceuticals, Inc.	34,998,000	1,392,920	-	-	-	(200,000)	-	
Comprehensive loss:								
Net loss	-	-	-	-	-	-	(3,699,491)	(3,69
Foreign currency translation adjustment	-	-	-	-	-	-	-	(
								(3,71

Comprehensive loss								
Balance, December 31, 2003	**99,968,840**	**$ 4,233,788**	**794,569**	**$ 350,484**	**$ -**	**$ (200,000)**	**$ (5,174,790)**	
Conversion of preferred stock to common stock	35,048,445	350,484	(794,569)	(350,484)	-	-	-	
Cash received from option exercise	-	-	-	-	-	200,000	-	
Stock issued in connection with bankruptcy	4,500,000	2,562,750	-	-	-	-	-	
Common stock issued in acquisition of Nanobac OY	5,000,000	4,267,500	-	-	-	-	-	
Capital contribution associated with sale subsidiary to affiliate	-	-	-	-	749,327	-	-	
Conversion of liabilities to shares of common stock	32,097,808	4,882,028	-	-	2,887,501	-	-	
Sale of common stock	10,625,000	-	-	-	(97,500)	-	-	
Comprehensive loss:								
Net loss	-	-	-	-	-	-	(7,874,778)	(7,87
Foreign currency translation adjustment	-	-	-	-	-	-	-	(
Derivative loss								(64
Comprehensive loss								(8,53

Balance, December 31, 2004	**187,240,093**	**$ 16,296,550**	**-**	**$ -**	**$ 3,539,328**	**$ -**	**$ (13,049,568)**

The accompanying notes are an integral part of these financial statements

NANOBAC PHARMACEUTICALS INCORPORATED AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS

	Year ended December 31, 2004	Year ended December 31, 2003
CASH FLOWS FROM OPERATING ACTIVITIES		
Net Loss	$ (7,874,778)	$ (3,699,491)
Adjustments to reconcile net loss to cash flows from operating activities:		
Depreciation and amortization	717,070	181,103
Loss on disposition of assets	-	7,659
Charges from common stock issuances	2,562,750	780,175
Minority interest in net loss	-	(3,545)
Interest expense added to stockholder loan	237,958	-
Net (increase) decrease in assets:		
Accounts receivable	2,370	9,125
Inventory	(54,360)	67,286
Other assets	(8,769)	78,383
Net increase (decrease) in liabilities:		
Accounts payable	530,196	278,107
Accrued compensation	464,768	46,658
Accrued expenses	10,628	99,218
Deferred revenue	16,423	-
Total adjustments	4,479,034	1,544,169
Net cash flows from operating activities	(3,395,744)	(2,155,322)
CASH FLOWS FROM INVESTING ACTIVITIES		
Acquisition of fixed assets	(36,765)	(18,157)
Security deposits	2,500	(2,932)
Acquisition of subsidiary, net of cash received	(901)	(81,022)
Cash received from exercise of stock option in subsidiary	200,000	300,000
Net cash flows from investing activities	164,834	197,889
CASH FLOWS FROM FINANCING ACTIVITIES		
Advances from line of credit, net	-	(36,453)
Proceeds from issuance of common stock and stock subscription agreements, net of expenses	1,177,500	548,000
Proceeds from stockholder loans, net	2,066,091	1,997,467
Payment of notes payable, net	(27,621)	(486,188)
Net cash flows from financing activities	3,215,970	2,022,826
Effect of exchange rate changes	(16,907)	(15,638)
Net change in cash	(31,847)	49,755
Cash balance, beginning of period	49,755	-

Cash balance, end of period	$	17,908	$	49,755
Supplemental disclosures of cash flow information:				
Cash paid for interest expense	$	10,095	$	42,934
Supplemental schedule of non-cash investing and financing activities:				
Common stock issued in acquisition	$	4,267,500	$	1,392,920
Common stock issued for the conversion of debt	$	7,769,529	$	728,800
Stockholder loan used for acquisition	$	-	$	4,071,342
Capital contribution associated with sale of subsidiary to affiliate Reduction in stockholder loan	$	250,000	$	-
Assumption of accounts payable and accrued expenses	$	499,327	$	-

The accompanying notes are an integral part of these financial statements

NANOBAC PHARMACEUTICALS, INCORPORATED AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
YEARS ENDED DECEMBER 31, 2004 AND 2003

1. Nature of operations and summary of significant accounting polices

Nature of business

Nanobac Pharmaceuticals, Incorporated and subsidiaries, ("Nanobac", the "Company", or "NNBP") trades under the symbol "NNBP."

NNBP's primary business is the study and development of therapeutic and diagnostic technologies related to nanobacterium sanguineum ("Nanobacteria"). Nanobacteria are believed to be small, slowly growing nano-particles that can be found in human blood, kidney stones and arterial wall plaques.

Principles of Consolidation

The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries. All material intercompany transactions and balances have been eliminated in consolidation. On June 4, 2003, the Company acquired a majority interest in NanobacLabs Pharmaceuticals, Inc. and on November 11, 2003, the Company acquired 65% of Nanobac OY (see Note 2, "Acquisitions"). In accordance with Statement of Financial Accounting Standards ("SFAS") No. 141, "Business Combinations", NNBP has included the results of operations of LABS from June 4, 2003 and the results of operations of OY from November 11, 2003.

Where losses applicable to the minority interest in a subsidiary exceed the minority interest in the equity capital of the subsidiary, such excess and any further losses applicable to the minority interest shall be charged against the majority interest, as there is no obligation of the minority interest to make good such losses.

Liquidity and Management Plans

The accompanying consolidated financial statements have been prepared assuming that NNBP will continue as a going concern. The Company has incurred recurring losses and has a working capital deficiency at December 31, 2004. The Company is dependent on the continued financing from outside investors including additional shareholder loans. All of these matters raise substantial doubt about the ability of the Company to continue as a going concern. Management believes that NNBP will need to raise additional capital in order to launch new clinical trials, fund research and development for new treatment areas, and general working capital requirements. Capital may be raised through further sales of equity securities, which may result in dilution of the position of current shareholders. At this time, there are no firm commitments to invest in NNBP. If NNBP is unable to obtain such financing, the business might not attain profitability.

There can be no assurances that NNBP will be successful in obtaining debt or equity financing in order to achieve its financial objectives and continue as a going concern. The financial statements do not include any adjustments to the carrying amount of assets and the amounts and classifications of liabilities that might result from the outcome of this uncertainty.

Revenue Recognition

Revenue is recognized when the Company's products are shipped and title has passed or when diagnostic results are provided to the customer. Revenue is recorded net of reserves for estimated discounts and incentives.

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NANOBAC PHARMACEUTICALS, INCORPORATED AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
YEARS ENDED DECEMBER 31, 2004 AND 2003

1. Nature of operations and summary of significant accounting polices (continued)

Financial instruments

The carrying value of NNBP's financial instruments, including cash, accounts receivable, accounts payable, short-term note payable and stockholder loans approximate their fair market values.

Inventory

Inventory is stated at the lower of cost or market. Cost is determined in a manner which approximates the first-in, first-out (FIFO) method. Inventory consists of raw materials for currently marketed products and materials and processing costs for antibodies and antigens used in our Finland laboratory. Inventory is shown net of applicable reserves and allowances. Shipping costs are expensed as incurred and are included in cost of revenue.

Fixed Assets

Fixed assets consist of furniture, fixtures, computers and lab equipment and are recorded at cost. Fixed assets are depreciated using the straight-line method over the estimated useful lives of three to seven years.

Intangible assets and goodwill

Intangible assets are recorded at cost, less accumulated amortization. Intangible assets consist of acquired technology rights obtained in the acquisition of LABS and OY (see Note 2). Amortization of intangible assets is provided over the following estimated useful lives on a straight-line basis:

Patents 12 years
Product rights 5 years

In accordance with Statement of Financial Accounting Standards No. 142, "Goodwill and Other Intangible Assets" ("SFAS No. 142"), and Statement of Financial Accounting Standards, No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets" ("SFAS No. 144"), the Company reviews its non-amortizable long-lived assets, including intangible assets and goodwill for impairment annually, or sooner whenever events or changes in circumstances indicate the carrying amounts of such assets may not be recoverable. Other depreciable or amortizable assets are reviewed when indications of impairment exist. Upon such an occurrence, recoverability of these assets is determined as follows. For long-lived assets that are held for use, the Company compares the forecasted undiscounted net cash flows to the carrying amount. If it is determined that the long-lived asset will be unable to recover its carrying amount, then it is written down to fair value. For long-lived assets held for sale, assets are written down to fair value. Fair value is determined based on discounted cash flows, appraised values for management's estimates, depending upon the nature or the assets. Impairment within goodwill is tested using a two step method. The first step is to compare the fair value of the reporting unit to its book value, including goodwill. If the fair value of the unit is less than its book value, the Company than determines the implied fair value of goodwill by deducting the fair value of the reporting unit's net assets from the fair value of the reporting unit. If the book value of goodwill is greater than its implied fair value, the Company writes down goodwill to its implied fair value. The Company's goodwill and intangible assets relate to the acquisition of NanobacLabs Pharmaceuticals, Inc. and Nanobac OY. Goodwill and intangible asset amortization is not deductible for income tax purposes.

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NANOBAC PHARMACEUTICALS, INCORPORATED AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
YEARS ENDED DECEMBER 31, 2004 AND 2003

1. Nature of operations and summary of significant accounting polices (continued)

Use of estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Net loss per share

Net loss per share represents the net loss attributable to common stockholders divided by the weighted average number of common shares outstanding during the period. The effect of incremental shares from common stock equivalents is not included in the calculation of net loss per share as the inclusion of such common stock equivalents would be anti-dilutive. Accordingly, fully dilutive shares outstanding equal basic shares outstanding as of December 31, 2004 and 2003.

NANOBAC PHARMACEUTICALS, INCORPORATED AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
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1. Nature of operations and summary of significant accounting polices (continued)

Accumulated Other Comprehensive Loss

Accumulated other comprehensive loss consists of derivative loss from derivative financial instruments and foreign currency translation adjustment related to our Finland operations. Accumulated other comprehensive income has no applicable income tax.

Derivative financial instruments

The Company accounts for derivative financial instruments indexed to and potentially settled in, its own stock in accordance with Emerging Issues Task Force 00-19, which provides that if the number of shares deliverable in a transaction be indeterminable, that said shares be presented as a liability in the balance sheet. Further, the liability is to be measured at fair value until such time as the obligation is settled. The shares issued in connection with the 2004 Subscription Agreement transactions discussed in Note 10 are derivative transactions and as such have been presented in the accompanying balance sheets as liabilities and other comprehensive income (loss). The other comprehensive income (loss) component represents the difference in the share value as issued and the value of said shares at the balance sheet date based on the trading value of the stock at December 31, 2004. At settlement, other comprehensive income (loss) will be charged to retained earnings as a constructive dividend.

Research and development expenses

Research and development expenses are comprised of the following types of costs incurred in performing R&D activities: salaries and benefits, occupancy costs of our Finland laboratory, professional fees, clinical trial and related clinical manufacturing costs. Research and development costs are expensed as incurred.

Income taxes

NNBP records its federal and state tax liability in accordance with Financial Accounting Standards Board Statement No. 109 “Accounting for Income Taxes”. The deferred taxes are recorded for temporary differences between the recognition of income and expenses for tax and financial reporting purposes, using current tax rates. Deferred assets and liabilities represent the future tax consequences of those differences, which will either be taxable or deductible when the assets and liabilities are recovered or settled.

NANOBAC PHARMACEUTICALS, INCORPORATED AND SUBSIDIARIES
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1. Nature of operations and summary of significant accounting polices (continued)

Recent accounting pronouncements

In November 2004, the FASB issued SFAS No. 151, "Inventory Costs." The statement amends Accounting Research Bulletin ("ARB") No. 43, "Inventory Pricing," to clarify the accounting for abnormal amounts of idle facility expense, freight, handling costs, and wasted material. ARB No. 43 previously stated that these costs must be "so abnormal as to require treatment as current-period charges." SFAS No. 151 requires that those items be recognized as current-period charges regardless of whether they meet the criterion of "so abnormal." In addition, this statement requires that allocation of fixed production overhead to the costs of conversion be based on the normal capacity of the production facilities. The statement is effective for inventory costs incurred during fiscal years beginning after June 15, 2005, with earlier application permitted for fiscal years beginning after the issue date of the statement. The adoption of SFAS No. 151 is not expected to have any significant impact on the Company's current financial condition or results of operations.

In December 2004, the FASB issued SFAS No. 153, "Exchanges of Nonmonetary Assets - An Amendment of APB Opinion No. 29." APB Opinion No. 29, "Accounting For Nonmonetary Transactions," is based on the opinion that exchanges of nonmonetary assets should be measured based on the fair value of the assets exchanged. SFAS No. 153 amends Opinion No. 29 to eliminate the exception for nonmonetary exchanges of similar productive assets and replaces it with a general exception for exchanges of nonmonetary assets whose results are not expected to significantly change the future cash flows of the entity. The adoption of SFAS No. 153 is not expected to have any impact on the Company's current financial condition or results of operations.

In December 2004, the FASB revised its SFAS No. 123 ("SFAS No. 123R"), "Accounting for Stock Based Compensation." The revision establishes standards for the accounting of transactions in which an entity exchanges its equity instruments for goods or services, particularly transactions in which an entity obtains employee services in share-based payment transactions. The revised statement requires a public entity to measure the cost of employee services received in exchange for an award of equity instruments based on the grant-date fair value of the award. That cost is to be recognized over the period during which the employee is required to provide service in exchange for the award. Changes in fair value during the requisite service period are to be recognized as compensation cost over that period. In addition, the revised statement amends SFAS No. 95, "Statement of Cash Flows," to require that excess tax benefits be reported as a financing cash flow rather than as a reduction of taxes paid. The provisions of the revised statement are effective for financial statements issued for the first interim or annual reporting period beginning after June 15, 2005, with early adoption encouraged. The Company is currently evaluating the impact that this statement will have on its financial condition or results of operations.

Reclassifications

Certain prior year amounts have been reclassified to conform to the current year presentation.

NANOBAC PHARMACEUTICALS, INCORPORATED AND SUBSIDIARIES
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2. Acquisitions

NanobacLabs Pharmaceuticals, Inc.

On June 4, 2003, NNBP acquired approximately 74.4% of LABS in exchange for 24,400,000 restricted shares of NNBP. From June 5, 2003 through December 31, 2003, NNBP acquired the remaining 25.6% of LABS from various stockholders in exchange for 6,598,000 restricted shares and additional consideration (in addition, see Note 10 for stock issued in connection with bridge funding for this acquisition).

The total consideration for LABS was approximately $5.5 million, which included the fair value of NNBP common stock issued, as well as direct transaction costs. The following table summarizes the estimated fair values of the assets acquired and liabilities assumed as of the acquisition date:

Current assets	$	895,058
Investment in OY		693,778
Fixed assets		113,651
Identifiable intangible assets		1,350,000
Goodwill		3,615,393
Other assets		62,500
Current liabilities		(768,280)
Note payable		(486,188)
	$	5,475,912

Acquired identifiable intangible assets consist of product rights for the treatment of Nanobacteria. The allocation of the purchase price was based, in part, on third-party valuations of the fair values of identifiable intangible assets. Amortization of this asset commenced as of the acquisition date.

NANOBAC PHARMACEUTICALS, INCORPORATED AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
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2. Acquisitions (continued)

Nanobac OY

Nanobac OY is a Finnish company that performs similar research to that of the Company in nanobacteria infection. On September 25, 2002, LABS entered into an agreement to purchase 27% of Nanobac OY stock from three Finnish entities for 11,430 Euros. A separate agreement also required LABS to acquire convertible promissory notes in Nanobac OY in the amount of 686,000 Euros plus interest. On November 11, 2003, NNBP completed the acquisition of Nanobac OY when the final payment was made and the Company exercised the conversion option in the convertible promissory notes. Upon the conclusion of this transaction, the Company owned 65% of OY.

During January through March 2004, NNBP acquired the remaining 35% of Nanobac OY from Dr. Kajander and Dr. Ciftcioglu ("OY Minority Shareholders"). The purchase price was (a) 5 million shares of NNBP's common stock, (b) 5 million warrants convertible into NNBP's common stock at $.005 per share and (c) cash consideration of 15,000 Euros. Total consideration to the OY Minority Stockholders is valued at $4.3 million.

The total consideration to date for OY is $5.1 million, which included cash payments (made before and after the acquisition of LABS), the fair value of NNBP common stock issued, as well as direct transaction costs. The following table summarizes the estimated fair values of the assets acquired and liabilities assumed as of the acquisition date:

Current assets	$	37,534
Fixed assets		29,286
Identifiable intangible assets		5,243,048
Other assets		4,731
Current liabilities		(11,884)
Advances from Nanobac		(228,119)
	$	5,074,596

Acquired identifiable intangible assets consist of patents for the detection and treatment of Nanobacteria. The allocation of the purchase price was based, in part, on third-party valuations of the fair values of identifiable intangible assets. Amortization of this asset commenced as of the acquisition date.

In addition, as part of the above agreement, the OY Minority Shareholders agreed to employment agreements with NNBP. These agreements included $500,000 of signing bonuses of which $150,000 was paid in 2004 and the remaining $350,000 (earned upon certain triggering events that occurred in 2004) is payable two years from the agreement dates (January and March 2006) and is included in long-term liabilities.

NANOBAC PHARMACEUTICALS, INCORPORATED AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
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2. Acquisitions (continued)

The following unaudited table compares NNBP's reported operating results to pro forma information prepared on the basis that the above acquisitions had taken place at January 1, 2003. In management's opinion, the unaudited pro forma combined results of operations are not indicative of the actual results that would have occurred had the acquisitions been consummated at the beginning of 2003 or 2004 or of future operations of the combined companies under the ownership and management of NNBP.

	Year ended December 31,	
	2004	2003
As Reported		
Revenue	$ 358,361	$ 482,815
Net loss	$ (7,874,778)	$ (3,699,491)
Basic loss per share	$ (0.05)	$ (0.05)
Diluted loss per share	$ (0.05)	$ (0.05)
Proforma		
Revenue	$ 358,361	$ 1,183,210
Net loss	$ (7,911,923)	$ (5,518,739)
Basic loss per share	$ (0.05)	$ (0.06)
Diluted loss per share	$ (0.05)	$ (0.06)

3. Discontinued Operations

During October 2003, NNBP decided to divest its HealthCentrics business unit to focus exclusively on its nanobacteria business unit. NNBP was unsuccessful in finding a non-affiliated buyer for this business unit. During March 2004, this business unit was sold to an affiliate of the current CEO for consideration of $250,000 (a reduction in amounts otherwise owed to the affiliate). NNBP's gain on disposal was $749,326, which is accounted for as a capital contribution given the related party nature of the arrangement. Summary operating results for the discontinued operations for the years ended December 31, 2004 and 2003 are as follows:

	2004	2003
Revenue	$ 5,301	$ 19,970
Loss before income taxes	($ 57,268)	($ 938,358)
Provision for income taxes	--	--
Net loss	($ 57,268)	($ 938,358)

NANOBAC PHARMACEUTICALS, INCORPORATED AND SUBSIDIARIES
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4. Fixed Assets

Fixed assets at December 31, 2004 are summarized as follows:

	Dec 2004
Computer equipment	$ 44,683
Computer software	17,982
Lab equipment	49,008
Office equipment	20,769
Furniture and fixtures	21,729
Leasehold improvements	54,967
	209,138
Accumulated Depreciation	(84,143)
	$ 124,995

Depreciation expense for the years ended December 31, 2004 and 2003 was $47,295 and $18,177, respectively.

5. Intangible Assets

Intangible assets as of December 31, 2004 are summarized as follows:

Product rights	$ 1,350,000
Patents	5,243,043
	6,593,043
Accumulated amortization	(832,701)
	$ 5,760,342

Amortization expense for the years ended December 31, 2004 and 2003 was $669,775 and $162,926, respectively. Expected future amortization is summarized as follows:

Year ending December 31,	
2005	$ 706,920
2006	706,920
2007	706,920
2008	549,420
2009	436,920
Thereafter	2,653,242
	$ 5,760,342

NANOBAC PHARMACEUTICALS, INCORPORATED AND SUBSIDIARIES
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6. Accrued Expenses

Accrued expenses as of December 31, 2004 are summarized as follows:

Accrued professional fees	$	79,500
Royalty		150,479
Employee expense reports		19,843
Payroll taxes and benefits		18,507
Other		67,532
	$	335,861

7. Segment Information

With the disposition of its HealthCentrics business unit (see Note 3), NNBP operates a single business segment. Geographic information is summarized as follows:

	Year ended December 31,	
	2004	2003
Revenue		
United States	$ 343,444	$ 472,735
Finland	14,917	10,080
	$ 358,361	$ 482,815
Assets		
United States	$ 3,281,026	
Finland	6,403,281	
	$ 9,684,307	

The geographic classification of revenue was based upon the domicile of the entity from which the revenues were earned. Approximately 98% of Finland assets relate to patents recorded as a result of the acquisition of OY (see Note 2).

NANOBAC PHARMACEUTICALS, INCORPORATED AND SUBSIDIARIES
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8. Income taxes

There was no current or deferred provision or benefit for income taxes for the years ended December 31, 2004 and 2003. The components of deferred tax asset as of December 31, 2004 and 2003 are as follows:

	2004	2003
Deferred tax asset:		
Net operating loss carryforwards	$ 3,690,000	$ 2,487,000
Valuation allowance	(3,690,000)	(2,487,000)
Deferred tax asset net of valuation allowance	$ -	$ -

As of December 31, 2004, the Company had approximately $9.1 million of net operating loss carryovers which expire between 2016 and 2024.

The following table accounts for the differences between the actual tax provision and the amounts obtained by applying the statutory U.S. federal income tax rates of 34% to the loss from continuing operations before income taxes and minority interest:

	2004	2003
Statutory tax benefit	$ 2,756,000	$ 967,000
State taxes, net of federal benefit	309,000	72,000
Nondeductible expense for common stock issued for services	(999,000)	(292,000)
Amortization of intangible assets	(261,000)	(57,000)
Nontaxable income in connection with HealthCentrics' disposition	305,000	-
Increase in valuation allowance	(2,116,000)	(715,000)
Other, net	6,000	25,000
Provision for taxes	$ -	$ -

Changes in the valuation allowance during the year ended December 31, 2004 were as follows:

Valuation allowance, beginning of year	$ 2,487,000
Discontinued operations	(913,000)
Increase from continuing operations	2,116,000
Valuation allowance, end of year	$ 3,690,000

NANOBAC PHARMACEUTICALS, INCORPORATED AND SUBSIDIARIES
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9. Related Party Transactions

Stockholder Loan

An entity controlled by the Chief Executive Officer (who is also the largest stockholder of NNBP), had loaned NNBP approximately $8.2 million from June 2003 through December 2004. This loan had interest at 5% and is due on demand. On September 30, 2004, $7.5 million of the above loan was converted into 29,999,964 shares of the Company's common stock. On December 13, 2004 an additional $500,000 of the above loan was converted into 4,166,667 shares of the of the Company's common stock, which is included in the Stock Settlement Liability at December 31, 2004 (see Note 10). The remaining loan balance at December 31, 2004 was approximately $194,000.

Interest expense for the above loans for the years ended December 31, 2004 and 2003 was approximately $238,000 and $23,000, respectively.

Short-Term Notes Payable

Short-term notes payable consist of unsecured advances from employees of the Company. These notes bear interest at 5% and are due on demand.

Conversion of Debt into Equity

During August 2004, an employee and minority stockholder (less than 5% ownership of the Company) converted an $111,000 liability due from the Company into 923,458 shares of the Company's common stock.

License Agreement

During February 2004, NNBP entered into a licensing agreement with Pegasus Worldwide, Inc. ("Pegasus") to market one of NNBP's over the counter products. NNBP's Chief Executive Officer is a director of Pegasus. Under the terms of the license agreement, NNBP was due $75 for each unit of product sold. For the year ended December 31, 2004, NNBP recognized revenue of $46,800 under this license agreement. Effective June 1, 2004, this license agreement was cancelled and NNBP is selling this product directly to customers.

Royalty Agreement

The Company was a party to a royalty agreement with the former majority owner of LABS who, along with his spouse, own approximately 24.4 million common shares of NNBP. Under the terms of the royalty agreement, this stockholder would receive an annual fee of $50,000 plus ten percent of gross sales from applicable products. On March 16, 2004, the U.S. Patent Office printed Patent 6,706,290 "Methods for Eradication of Nanobacteria". With the approval of this patent, management believes that the above royalty agreement is not valid and no amounts will ultimately be due under the above royalty agreement.

NANOBAC PHARMACEUTICALS, INCORPORATED AND SUBSIDIARIES
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10. Stockholders' equity

Preferred stock

The holder(s) of preferred shares are entitled to receive non-cumulative dividends not to exceed $.10 per share when and as declared by the Board of Directors. In the event of any liquidation, dissolution or winding down of the company, either voluntary or involuntary, the holder(s) of each preferred share shall be entitled to be paid on an amount equal to $4.00 per share. In the event that the Company authorizes the redemption of all or any preferred shares, the redemption price shall be $4.30 per share. The preferred shares are convertible at any time into common at the ratio of 44.11 common shares to one preferred share. Holders of preferred shares have a right to cast eight votes per preferred share and the right to elect 50% of the authorized members of the board of directors.

Common stock, preferred stock and warrant issuances

During 2004, creditors of the Company converted $7.8 million of liabilities into 32,097,808 shares of the Company's common stock as follows:

Shareholder loan (Note 9)	29,999,964	$	7,499,990
Employee (Note 9)	923,458		110,815
Unaffiliated vendors	1,174 385		158,724
	32,097,807	$	7,769,529

During 2004, the Company issued 5.0 million shares of its common stock and 5.0 million warrants with an exercise price of $0.005 per share in connection with the acquisition of the minority interest in OY (see Note 2). The value of these stock and stock equivalent issuances was $4.3 million.

From August 2004 through November 2004, the Company entered into Subscription Agreements with two unaffiliated investors. Under the terms of the Subscription Agreements, the Company received cash of $677,500 (net of $97,500 of expenses) during the year ended December 31, 2004. The Company is to receive additional cash of $775,000 within five days of registering the common shares and warrants issued as a result of the Subscription Agreements. The number of common shares to be issued is equal to the amount received divided by the lesser of $.12 or 52% of the average closing bid price of the Company's common stock on the five trading days immediately prior to the date on which the registration statement is declared effective ("Fixed Price"). These amounts are classified as Stock Settlement Liability at December 31, 2004. In addition, the Subscription Agreements provide for the issuance of warrants equal to the number of common shares issued. Fifty percent (50%) of the warrants are exercisable at 110% of the Fixed Price and the remaining 50% of the warrants are exercisable at 150% of the Fixed Price. Unexercised warrants will expire December 31, 2008. The Company has agreed to use its best efforts to promptly register the common shares and warrants.

During December 2004, the Company entered into a Subscription Agreement with an affiliate of the Company's Chief Executive Officer. Under the terms of the Subscription Agreement, the Company received cash of $500,000 during the year ended December 31, 2004. The Company is to receive additional cash of $500,000 within five days of registering the common shares and warrants issued as a result of the Subscription Agreement. All other terms of the Subscription Agreement are substantially the same as the Subscription Agreements to the unaffiliated investors described in the preceding paragraph. This amount is classified as Stock Settlement Liability at December 31, 2004.

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10. Stockholders' equity (continued)

As a result of the above Subscription Agreements, at December 31, 2004, the Company has issued 10,625,000 shares of common shares, which represents the minimum number of shares to be issued under the Subscription Agreements in exchange for cash received through December 31, 2004. If the price of the Company's stock is less than $0.23 per share when the Company's registration statement is declared effective, the Company will be required to issue additional shares under the above Subscription Agreements equal to a price of 52% of the average closing bid price of the Company's common stock on the five trading days immediately prior to the date on which the registration statement is declared effective. The ultimate number of shares to be issued is indeterminate as the number of shares is dependent on NNBP's closing bid price when a registration statement is declared effective. As a result, the $1,275,000 of cash received under the Subscription Agreements through December 31, 2004 is included in long-term liabilities.

At December 31, 2004, the Company measured the value of the shares to be issued under the Subscription Agreements through December 31, 2004 based on the Company's closing bid price at December 31, 2004 compared to the actual shares issued. As a result of this measurement, an additional $643,630 long-term liability was recorded as of December 31, 2004 with a charge to Other Comprehensive Income.

From May 2001 through November 2002, the Company was subject to the jurisdiction of the United States Bankruptcy Court ("the Bankruptcy Court") under Chapter 11 of the United States Bankruptcy Code. Throughout the bankruptcy proceedings, the Company's CEO and an affiliated entity funded the Company's operations and existence. As part of the plan of reorganization as approved by the Bankruptcy Court, the Company was to issue 75 million shares of the Company's stock to affiliates of the CEO in satisfaction of this obligation. This transaction was recorded at $750,000 or $.01 per share fair value at the date of the award (based on the value at the measurement date) although shares were issued periodically throughout 2003. Certain shares were issued as preferred shares (at an equivalent value based on the conversion ratio of 44.11 per share). During January 2004, the number of authorized shares was increased to 250,000,000, at which time the previously issued preferred stock was converted to 35,048,445 shares of common stock.

During January 2004, a remaining Bankruptcy obligation was satisfied when the Company issued 4.5 million common shares to an entity that is an affiliate of the Company's CEO. The Company recognized an expense of $2.6 million in 2004 in connection with this 4.5 million stock issuance which is the approximate fair value of the stock on the issuance date.

During 2003, a total of 34,998,000 shares of the Company's common stock were issued for the acquisition of LABS (see Note 2) including 4.0 million common shares to an affiliate of the Company's Chief Executive Officer in connection with the facilitation and bridge funding for this acquisition. The value of these share issuances was approximately $1.4 million.

An aggregate of 3,644,000 shares of stock were issued during 2003 in connection with the conversion of $728,800 in related party debt to equity. Stock issued for services in 2003 aggregated 50,000 shares valued at $30,175.

In addition, the Company sold 1,690,000 shares of stock at prices ranging from $.20 to $.40 for aggregate proceeds of $548,000 and 368,815 shares of preferred stock were converted to 16,268,430 shares of common stock.

NANOBAC PHARMACEUTICALS, INCORPORATED AND SUBSIDIARIES
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10. Stockholders' equity (continued)

Warrants

As of December 31, 2004, in connection with the OY acquisition, 5,000,000 warrants were outstanding with an exercise price of $.005 per common share and an expiration date of August 31, 2009 (see Note 2).

At the finalization of the Subscription Agreements described above, approximately 23.4 million additional warrants will be issued with an estimated weighted average exercise price of $.16 per common share and an expiration date of five years from the date of issuance.

Stock Option Plan

No stock options were outstanding for the years ended December 31, 2004 and 2003.

11. Commitments

The Company leases administrative and laboratory facilities and office equipment under cancelable and non-cancelable operating leases that expire through June 2010. The following table summarizes the minimum future rental commitments under non-cancelable operating leases at December 31, 2004:

Year ending December 31,		
2005	$	174,281
2006		178,408
2007		109,225
2008		58,163
2009		53,900
2010		27,234
	$	601,211

Rent expense on operating leases for the years ended December 31, 2004 and 2003 was approximately $222,000 and $167,000, respectively.

NANOBAC PHARMACEUTICALS, INCORPORATED AND SUBSIDIARIES
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13. Contingency

On September 24, 2004 a civil action was filed in United States District Court - Southern District of California by World Health Products, LLC (“World Health”) broadly alleging that the Company, together with a customer of the Company (“Customer”), has infringed on its Patent Number 5,602,180 related to the sale of suppositories included in the Company’s supplement product. World Health alleged additional complaints against the Customer to which the Company is not liable. During February 2005, World Health dropped the Company from their lawsuit as their tests of the Company’s suppositories determined that World Health’s patents were not being infringed upon.

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15. Quarterly Data

	Mar 31	Jun 30	Sep 30	Dec 31
2004 Quarter ended				
Revenue	$ 32,385	$ 73,564	$ 118,141	$ 134,271
Gross profit	$ 25,196	$ 42,072	$ 76,037	$ 114,586
Loss from continuing operations	($4,221,972)	($1,384,238)	($994,276)	($1,217,024)
Net loss	($4,279,240)	($1,384,238)	($994,276)	($1,217,024)
Loss per share:				
Basic and Diluted	($0.03)	($0.01)	($0.01)	($0.00)
2003 Quarter ended				
Revenue	$ 0	$ 77,637	$ 241,340	$ 163,838
Gross profit	$ 0	$ 17,174	$ 63,932	$ 68,587
Loss from continuing operations	($935,446)	($166,229)	($679,241)	($980,217)
Net loss	($1,234,083)	($468,666)	($929,230)	($1,067,512)
Loss per share:				
Basic and Diluted	($0.03)	($0.01)	($0.01)	($0.01)

Reconciliation of 2003 Quarterly Data to Forms 10-QSB as filed

	Mar 31	Jun 30	Sep 30
Revenue			
Revenue as reported on Form 10Q	$ 5,812	$ 84,049	$ 244,616
Discontinued operations	(5,812)	(6,412)	(3,276)
Revenue per above	$ 0	$ 77,637	$ 241,340
Gross Profit			
Gross profit as reported on Form 10Q	($10,300)	$ 3,034	$ 38,503
Discontinued operations	10,300	14,140	25,429
Gross profit per above	$ 0	$ 17,174	$ 63,932
Net loss			
Net loss as reported on Form 10Q	($595,222)	($449,924)	($913,780)
Amortization of intangible assets	-	(18,742)	(90,000)
Charge or reversal thereof for stock issuances to affiliates of officers	(650,000)		74,550
Other	11,139	-	-
Net loss per above	($1,234,083)	($468,666)	($929,230)