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I TRAX INC
Form 10QSB/A
December 16, 2004

UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-QSB/A

(Mark One)

QUARTERLY REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended: September 30, 2004

TRANSITION REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT

Commission File Number: 001-31584

I-TRAX, INC.

(Exact name of small business issuer as specified in its charter)

Delaware

(State or other jurisdiction of incorporation or organization)

23-3057155

(I.R.S. Employer Identification No.)

4 Hillman Drive, Suite 130
Chadds Ford, Pennsylvania 19317

(Address of principal executive offices)

(610) 459-2405

(Issuer's telephone number)

One Logan Square, 130 N. 18th Street, Suite 2615
Philadelphia, Pennsylvania 19103

(Former name, former address and former fiscal year,
if changed since last report)

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

State the number of shares outstanding of each of the issuer's classes of common equity, as of the latest practicable date: As of November 11, 2004, the number of outstanding shares of common stock, par value \$.001 per share, was 28,655,871.

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

EXPLANATORY NOTE

This amendment amends I-trax, Inc.'s Quarterly Report on Form 10-QSB for the quarter ended September 30, 2004 filed with the Securities and Exchange Commission on November 15, 2004. The purpose of this amendment is to amend the following:

- o Disclosure of number of shares of common stock issuable upon exercise of options, warrants and convertible preferred stock excluded from the diluted loss per share computation presented in Note 2 of the notes to I-trax's condensed consolidated financial statements (unaudited);
- o Disclosure of options granted during the three month period ended September 30, 2004 presented in Note 8 of the notes to I-trax's condensed consolidated financial statements (unaudited); and
- o Supplemental disclosure of pro forma net loss per share under SFAS No. 123 presented in Note 8 of the notes to I-trax's condensed consolidated financial statements (unaudited).

The Quarterly Report on Form 10-QSB for the quarter ended September 30, 2004 filed with the Securities and Exchange Commission on November 15, 2004 reflected grants of options to acquire an aggregate of 1,742,000 shares of I-trax common stock during the three month period ended September 30, 2004. Following consultation with its professional advisors, I-trax has concluded that these options were not validly granted, and therefore not outstanding, because, among other reasons, the grants were not made in compliance with I-trax's 2001 Equity Compensation Plan and applicable Internal Revenue Code regulations. I-trax expects its Board of Directors to validly grant these options as soon as reasonably practicable on terms approved by the Board.

Except as described above, no other changes have been made to I-trax's Quarterly Report on Form 10-QSB for the quarter ended September 30, 2004 filed on November 15, 2004.

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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

I-TRAX, INC.
INDEX TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

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Report of Independent Registered Public Accounting Firm

To the Board of Directors and Stockholders
of I-trax, Inc.

We have reviewed the accompanying condensed consolidated balance sheet of I-trax, Inc. (a Delaware corporation) and Subsidiaries as of September 30, 2004, and the related condensed consolidated statements of operations for the three month and nine month periods ended September 30, 2004 and 2003, the condensed consolidated statements of stockholders' equity for the nine month period ended September 30, 2004 and the condensed consolidated statements of cash flows for the nine month periods ended September 30, 2004 and 2003. These interim financial statements are the responsibility of the company's management.

We conducted our reviews in accordance with the standards of the Public Company Accounting Oversight Board (United States). A review of interim financial information consists principally of applying analytical procedures and making inquiries of persons responsible for financial and accounting matters. It is substantially less in scope than an audit conducted in accordance with the standards of the Public Company Accounting Oversight Board, the objective of

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which is the expression of an opinion regarding the condensed consolidated financial statements taken as a whole. Accordingly, we do not express such an opinion.

Based on our reviews, we are not aware of any material modifications that should be made to the condensed consolidated financial statements referred to above for them to be in conformity with United States generally accepted accounting principles.

We have previously audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the balance sheet as of December 31, 2003, and the related consolidated statements of operations, stockholders' equity and cash flows for the year then ended (not presented herein); and in our report dated February 16, 2004, we expressed an unqualified opinion on those financial statements. In our opinion, the information set forth in the accompanying condensed consolidated balance sheet as of December 31, 2003 is fairly stated, in all material respects, in relation to the consolidated balance sheet from which it has been derived.

GOLDSTEIN GOLUB KESSLER LLP
New York, New York

October 27, 2004

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I-TRAX, INC. AND SUBSIDIARIES CONDENSED CONSOLIDATED BALANCE SHEETS (in thousands, except share data)

	ASSETS	September 30, 2004 (unaudited) -----
Current assets		
Cash and cash equivalents		\$ 5,453
Accounts receivable, net		12,363
Income tax receivable		132
Other current assets		2,105

Total current assets		20,053
Property and equipment, net		5,784
Goodwill		46,064
Customer list, net		28,374
Other intangible assets, net		1,805
Other long term assets		113

Total assets		\$ 102,193 =====

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LIABILITIES AND STOCKHOLDERS' EQUITY

Current liabilities	
Accounts payable	\$ 6,024
Accrued expenses	4,765
Due to officers and related parties	--
Notes payable	2,000
Net liabilities of discontinued operations	1,299
Other current liabilities	8,730

Total current liabilities	22,818
Common stock warrants	--
Note payable	5,500
Other long term liabilities	2,437

Total liabilities	30,755

Commitments and contingencies	--
Stockholders' equity	
Preferred stock - \$.001 par value, 2,000,000 shares authorized, 1,200,000 and -0- issued and outstanding, respectively	1
Common stock - \$.001 par value, 100,000,000 shares authorized, 24,796,671 and 13,966,817 shares issued and outstanding, respectively	24
Additional paid in capital	130,593
Accumulated deficit	(59,180)

Total stockholders' equity	71,438

Total liabilities and stockholders' equity	\$ 102,193
	=====

See accompanying notes to consolidated financial statements (unaudited)

I-TRAX, INC. AND SUBSIDIARIES
 CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
 FOR THE THREE MONTHS ENDED SEPTEMBER 30, 2004 AND 2003
 (UNAUDITED)
 (in thousands, except share data)

Three months ended September 30,	Three mont ended September
--	----------------------------------

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	2004	2003
	-----	-----
Net revenue	\$ 24,136	\$ 1,0
	-----	-----
Costs and expenses:		
Operating expenses	18,816	6
General and administrative expenses	4,670	1,0
Depreciation and amortization	1,097	4
	-----	-----
Total costs and expenses	24,583	2,1
	-----	-----
Operating loss	(447)	(1,1
	-----	-----
Other expenses (income):		
Interest expense	124	9
Amortization of financing costs	13	(5
Other income	--	(5
	-----	-----
Total other expenses	137	5
	-----	-----
Loss before provision for income taxes	(584)	(1,6
	-----	-----
Provision for income taxes	251	
Net loss	(835)	(1,6
	-----	-----
Less preferred stock dividend	(605)	
	-----	-----
Net loss applicable to common stockholders	\$ (1,440)	\$ (1,6
	=====	=====
Loss per common share, basic and diluted	\$ (0.06)	\$ (0.
	=====	=====
Weighted average number of shares outstanding, basic and diluted	24,730,933	11,121,7
	=====	=====

See accompanying notes to consolidated financial statements (unaudited).

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FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2004 AND 2003

(UNAUDITED)

(in thousands, except share data)

	Nine months ended September 30, 2004	Nine months ended September 30, 2003
	-----	-----
Net revenue	\$ 49,968	\$
	-----	-----
Costs and expenses:		
Operating expenses	38,631	
General and administrative expenses	11,342	
Depreciation and amortization	2,889	
	-----	-----
Total costs and expenses	52,862	
	-----	-----
Operating loss	(2,894)	(
	-----	-----
Other expenses (income):		
Interest expense	900	
Amortization of financing costs	60	
Other expenses (income)	350	
	-----	-----
Total other expenses	1,310	
	-----	-----
Loss before provision for income taxes	(4,204)	(
	-----	-----
Provision for income taxes	251	
	-----	-----
Net loss	(4,455)	(
	-----	-----
Less preferred stock dividend	(1,282)	
	-----	-----
Less deemed dividends applicable to preferred stockholders	(15,820)	
	-----	-----
Net loss applicable to common stockholders	\$ (21,557)	\$ (
	=====	=====
Loss per common share, basic and diluted:	\$ (1.00)	\$
	=====	=====
Weighted average number of shares outstanding, basic and diluted:	21,613,701	10,11
	=====	=====

See accompanying notes to consolidated financial statements (unaudited).

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I-TRAX, INC. AND SUBSIDIARIES
 CONDENSED CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY
 FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2004
 (UNAUDITED)
 (in thousands, except share data)

	Preferred Stock		Common Stock	
	Shares	Amount	Shares	Amount
Balances at January 1, 2004	--	\$ --	13,966,817	\$ 14
Reclassification of common stock warrants to paid in capital	--	--	--	--
Issuance of common stock in connection with conversion of promissory note and other settlement, net of costs	--	--	69,165	--
Issuance of common stock for conversion of debenture and accrued interest	--	--	427,106	--
Issuance of common stock for exercise of warrants	--	--	333,583	--
Sale of preferred stock, net of costs	1,000,000	1	--	--
Issuance of preferred stock for acquisition of CHD Meridian	400,000	--	--	--
Redemption of preferred stock	(200,000)	--	--	--
Issuance of common stock for acquisition of CHD Meridian	--	--	10,000,000	10
Beneficial conversion feature in connection with issuance of preferred stock	--	--	--	--
Preferred stock dividend	--	--	--	--
Net loss for the nine months ended September 30, 2004	--	--	--	--
Balances at September 30, 2004	1,200,000	\$ 1	24,796,671	\$ 24

See accompanying notes to consolidated financial statements (unaudited)

I-TRAX, INC. AND SUBSIDIARIES
 CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
 FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2004 AND 2003
 (UNAUDITED)
 (in thousands, except share data)

	Nine months ended September 30, 2004 -----
Operating activities:	
Net loss	\$ (4,455)
Adjustments to reconcile net loss to net cash provided by (used in) operating activities:	
Depreciation and amortization	2,889
Accretion of discount on notes payable charged to interest expense and beneficial conversion value of debenture	573
Increase in fair value of common stock warrants	350
Amortization of debt issuance costs	47
Write-off of deposit on cancelled acquisition	--
Issuance of securities for services	--
Other non-cash items	--
Changes in operating assets and liabilities, net of acquisition:	
Decrease in accounts receivable	996
Decrease in income tax receivable	147
Increase in other current assets	(920)
Increase in other long term assets	(52)
Decrease in accounts payable	(948)
Increase in accrued expenses	1,463
(Decrease) increase in other current liabilities	260

Net cash provided by (used in) operating activities	350

Investing activities:	
Purchases of property, plant and equipment	(1,628)
Acquisition of intangible assets	(688)
Acquisition of CHD Meridian, net of acquired cash	(18,134)

Net cash used in investing activities	(20,450)

Financing activities:	
Principal payments on capital leases	(35)
Proceeds from/ repayment to related parties	(280)
Proceeds (repayment) of note payable	(618)
Proceeds from exercise of warrants	52
Proceeds from bank credit facility, net of issuance costs	7,350
Proceeds from sale of preferred stock, net of issuance costs	23,510
Proceeds from sale of common stock	--

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Redemption of preferred stock	(5,000)

Net cash provided by financing activities	24,979

Net increase (decrease) in cash and cash equivalents	4,879
Cash and cash equivalents at beginning of period	574

Cash and cash equivalents at end of period	\$ 5,453
	=====
Supplemental disclosure of non-cash flow information:	
Cash paid during the year for:	
Interest	\$ 377
	=====

(Continues on following page.)

See accompanying notes to consolidated financial statements (unaudited).

I-TRAX, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENT OF CASH FLOWS
FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2004 AND 2003

(Continues from previous page.)

	Nine months ended September 30, 2004

Income taxes	\$ 257
	=====
Schedule of non-cash financing activities:	
Reclassification of common stock warrants to paid in capital	\$ 3,110
	=====
Issuance of common stock in connection with conversion of promissory note and other settlement	\$ 71
	=====
Issuance of common stock in connection with conversion of debenture payable	\$ 747
	=====
Beneficial conversion feature in connection with issuance of preferred stock	\$ 15,820
	=====

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Issuance of common and preferred stock in connection with the acquisition of CHD Meridian	\$ 46,300 =====
Preferred stock dividend	\$ 1,282 =====
Issuance of common stock in connection with the conversion of deferred salaries	\$ -- =====
Purchase of all capital stock of CHD Meridian and assumption of liabilities in the acquisition as follows:	
Fair value of non-cash tangible assets acquired	\$ 17,257
Goodwill	37,429
Customer list	29,184
Other intangibles	1,167
Cash paid, net of cash acquired (includes \$85 of transaction costs incurred in a prior period)	(18,834)
Common stock issued	(36,300)
Preferred stock issued	(10,000)
	=====
Liabilities assumed	\$ (19,903) =====

See accompanying notes to consolidated financial statements (unaudited).

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I-TRAX, INC. AND SUBSIDIARIES NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

NOTE 1--ORGANIZATION

I-trax, Inc. (the "Company") was incorporated in the State of Delaware on September 15, 2000. On March 19, 2004, the Company consummated a merger with Meridian Occupational Healthcare Associates, Inc., a private company, which does business as CHD Meridian Healthcare ("CHD Meridian"). (See Note 3--Business Combination.)

Following the merger, the Company offers two categories of services: (1) on-site health related services such as occupational health, primary care, corporate health, and pharmacy; and (2) personalized health management programs.

The Company conducts its on-site services through CHD Meridian Healthcare, LLC, a Delaware limited liability company ("CHD Meridian LLC"), and its subsidiary companies, and its personalized health management programs through I-trax Health Management Solutions, LLC, a Delaware limited liability company, and I-trax Health Management Solutions, Inc., a Delaware corporation.

Physician services at the Company's on-site locations are provided under management agreements with affiliated physician associations, which are organized professional corporations that hire licensed physicians who provide medical services (the "Physician Groups"). The Physician Groups provide all

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medical aspects of the Company's on-site services, including the development of professional standards, policies and procedures. The Company provides a wide array of business services to the Physician Groups, including administrative services, support personnel, facilities, marketing, and non-medical services.

NOTE 2--INTERIM RESULTS AND BASIS OF PRESENTATION

The accompanying unaudited financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information and the instructions to Form 10-QSB and Item 310(b) of Regulation S-B promulgated under the Securities Exchange Act of 1934. In the opinion of management, the unaudited financial statements have been prepared on the same basis as the annual financial statements and reflect all adjustments necessary to present fairly the financial position as of September 30, 2004 and the results of the operations and cash flows for the three and nine months ended September 30, 2004. Because the combination of the Company and CHD Meridian for accounting purposes was effective as of April 1, 2004, the results for the nine months ended September 30, 2004 only include the operations of CHD Meridian for the six months ended September 30, 2004. The balance sheet at December 31, 2003 has been derived from the audited financial statements of the Company at that date.

Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been condensed or omitted pursuant to the Securities and Exchange Commission's rules and regulations.

Loss per common share is computed pursuant to SFAS No. 128, "Earnings Per Share." Basic loss per share is computed as net income (loss) available to common stockholders divided by the weighted average number of common shares outstanding for the period. Diluted loss per share reflects the potential dilution that could occur from common shares issuable through stock options, warrants and convertible preferred stock. As of September 30, 2004 and 2003, 17,168,561 and 5,809,093 shares issuable upon exercise of options, warrants and convertible preferred stock, respectively, were excluded from the diluted loss per share computation because their effect would be anti-dilutive.

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I-TRAX, INC. AND SUBSIDIARIES NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

NOTE 2--INTERIM RESULTS AND BASIS OF PRESENTATION (continued)

These unaudited financial statements should be read in conjunction with the Company's audited financial statements for the year ended December 31, 2003 included in the Company's annual report on Form 10-KSB/A filed on August 11, 2004, and the financial statements of CHD Meridian and notes thereto included in the Company's current report on Form 8-K/A filed on November 10, 2004.

The consolidated financial statements include the balance sheet of CHD Meridian LLC, its wholly owned subsidiaries, the Physician Groups and Green Hills

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Insurance, a risk retention group (see Note 9- Risk Retention Group). The financial statements of the Physician Groups are consolidated with CHD Meridian LLC in accordance with the nominee shareholder model of Emerging Issues Task Force ("EITF") Issue No. 97-2, "Application of FASB Statement No. 94 and APB Opinion No. 16 to Physician Practice Management Entities and Certain Other Entities with Contractual Management Arrangements." CHD Meridian LLC has unilateral control over the assets and operations of the Physician Groups. Control of the Physician Groups is perpetual and other than temporary because of the nominee shareholder model and the management agreements between the entities. The net tangible assets of the Physician Groups were not material at September 30, 2004.

The Company records pass-through pharmaceutical purchases on a net basis in compliance with EITF Issue No. 99-19, "Reporting Gross Revenue as a Principal vs. Net as an Agent." The amounts of pass-through pharmaceuticals purchased by the Company for the three and nine months ended September 30, 2004 were \$25,357,000 and \$50,228,000, respectively.

For comparability, certain 2003 amounts have been reclassified to conform to the financial statement presentation used in 2004.

As shown in the accompanying financial statements, the Company has suffered recurring losses from operations, has an accumulated deficit, and a working capital deficiency. The Company borrowed funds under its senior secured credit facility (see Note 6 - Long Term Debt) and has entered into agreements with new customers which management expects to provide increased revenue. The Company believes these measures will sustain operations through December 31, 2004.

NOTE 3--BUSINESS COMBINATION

On March 19, 2004, the Company merged with CHD Meridian, a privately held company and a major provider of outsourced, employer-sponsored healthcare services. CHD Meridian provides such services to large self-insured employers, including Fortune 1,000 companies.

Pursuant to the merger agreement, the Company, (1) issued 10,000,000 shares of common stock, (2) issued 400,000 shares of convertible preferred stock (with each share convertible into 10 shares of common stock) at \$25.00 per share or \$10,000,000 in the aggregate, and (3) paid approximately \$25,508,000 in cash to the CHD Meridian stockholders. Immediately following the closing of the merger, the Company also redeemed from former CHD Meridian stockholders that participated in the merger, pro rata, an aggregate of 200,000 shares of convertible preferred stock at its original issue price of \$25.00 per share or \$5,000,000. The total value of the merger consideration is \$73,592,000, made up of common stock valued at \$36,300,000, preferred stock valued at \$10,000,000, cash of \$25,908,000 and transaction expenses of \$1,384,000. The Company has filed a registration statement with the Securities and Exchange Commission to register for resale the (a) common stock issued in the merger, and (b) common stock issuable upon conversion of convertible preferred stock issued in the merger.

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NOTE 3--BUSINESS COMBINATION (continued)

The former CHD Meridian stockholders will also receive additional shares of the Company's common stock if CHD Meridian, continuing its operations following the closing of the merger as CHD Meridian LLC, achieves calendar 2004 milestones for earnings before interest, taxes, depreciation and amortization (or EBITDA) as follows: If EBITDA equals or exceeds \$8,100,000, the number of such additional common shares payable will be 3,473,280; the number of such shares will increase proportionately with EBITDA above \$8,100,000, up to a maximum of 3,859,200 additional shares of the Company's common stock if EBITDA equals or exceeds \$9,000,000. In connection with this earn-out, the Company placed 3,859,200 shares in escrow. The shares are not recorded as outstanding for accounting purposes until the earn-out target is satisfied.

The Company funded the cash portion of the merger consideration by (1) selling 1,000,000 shares of convertible preferred stock at \$25.00 per share (with each share convertible into 10 shares of common stock), for gross proceeds of \$25,000,000, and (2) drawing \$12,000,000 under a new senior secured credit facility with a national lender. (See Note 6 - Long Term Debt.)

In connection with the sale and issuance of the convertible preferred stock, the Company reported \$15,820,000 as a deemed dividend to preferred stockholders representing the beneficial conversion value for the underlying common stock as of the date of the merger agreement. The beneficial conversion value is treated as a dividend on the convertible preferred stock solely for the purpose of computing earnings per share. The dividend is computed by multiplying (1) the difference between the value of the underlying common stock calculated using the average closing price for the three days prior and three days after the announcement of the merger (\$3.63 per share) and the conversion price (\$2.50 per share) by (2) the number of shares of common stock into which the convertible preferred stock outstanding at the merger's effective time was convertible (14,000,000 shares).

The acquisition was accounted for using the purchase method of accounting. The Company incurred acquisition costs of \$1,384,000 that are included in the purchase price. In addition, \$832,000 of transaction related bonuses and termination pay are included in the general and administrative expense item on the condensed consolidated statement of operations.

The aggregate purchase price of \$73,592,000 for this transaction is summarized as follows:

Fair value of tangible assets acquired (includes cash of \$8,444,000)	\$ 25,715,000
Liabilities assumed	(19,903,000)
Goodwill	37,429,000
Customer list	29,184,000
Other intangibles	1,167,000
	\$ 73,592,000
	\$ 73,592,000

The following are the Company's unaudited pro forma results of operations giving effect to the acquisition of CHD Meridian as though the transaction had occurred on January 1, 2003. The results exclude transaction costs of \$1,938,000 and transaction related bonuses and termination pay of \$832,000 included in the CHD Meridian and the Company's statements of operations, respectively. The pro forma results also include adjustments to amortization expense associated with the intangibles acquired and interest expense related to the new senior secured credit facility.

I-TRAX, INC. AND SUBSIDIARIES
 NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
 (UNAUDITED)

NOTE 3--BUSINESS COMBINATION (continued)

	Nine months ended September 30, 2004	Nine months ended September 30, 2003
	-----	-----
Net revenue	73,322,000	73,018,000
	-----	-----
Operating loss	(1,453,000)	(1,070,000)
	-----	-----
Net loss	(3,166,000)	(4,253,000)
	=====	=====
Loss per share	(0.13)	(0.21)
	=====	=====

NOTE 4--GOODWILL AND INTANGIBLE ASSETS

During the quarter ended September 30, 2004, goodwill increased by \$211,000. This increase is related to the cost of continuing directors and officers' insurance coverage for former directors and officers of CHD Meridian. The changes in the carrying amount of goodwill for the nine months ended September 30, 2004 are as follows:

	Total

Balance as of January 1, 2004	\$ 8,424,000
Goodwill acquired in the nine months ended September 30, 2004	37,640,000

Balance as of September 30, 2004	46,064,000
	=====

The components of identifiable intangible assets, which are included in the consolidated balance sheet as of September 30, 2004, are as follows:

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	Gross Carrying Amount	Accumulated Amortization	Net A
	-----	-----	-----
Amortized intangible assets:			
Customer lists	36,492,000	8,118,000	
Other intangibles	5,124,000	3,319,000	
	-----	-----	-----
Total	41,616,000	11,437,000	
	=====	=====	=====

Customer lists are amortized on a straight-line basis over the expected periods to be benefited, generally 12 to 15 years. Other intangible assets represent technology and deferred marketing costs, which are amortized on a straight-line basis over the expected periods to be benefited, generally 3 to 5 years. In accordance with SFAS No. 142, the Company completes a test for impairment of goodwill and certain other intangible assets annually.

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I-TRAX, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

NOTE 5--CONVERTIBLE DEBENTURE

During the first quarter of 2004, Palladin Opportunity Fund LLC converted the remaining balance of the debenture payable and accrued interest into common stock. Accordingly, the Company issued 427,106 shares of common stock for the conversion of principal and accrued interest amounting to \$747,000.

Interest expense associated with the convertible debenture amounted to \$368,000 for the nine months ended September 30, 2004. This amount includes \$362,000 that represents accelerated accretion to interest expense for the discount of the value assigned to the warrants issued to the debenture holder and the beneficial conversion value at date of issuance.

NOTE 6--LONG TERM DEBT

On March 19, 2004, in connection with the CHD Meridian acquisition, the Company obtained a \$20,000,000 senior secured credit facility from a national lender. The credit facility expires on April 1, 2007. The credit facility originally had a \$6,000,000 term loan commitment with a \$14,000,000 revolving credit commitment. Outstanding letters of credit liabilities reduce the amount available to be borrowed under the revolving credit commitment. The credit facility has subsequently been amended, as discussed below.

In addition to funding the merger and related costs, the Company used a portion of the proceeds from the credit facility to repay \$280,000 in related party loans and \$944,000 in principal and interest for all other outstanding promissory notes.

The credit facility is secured by substantially all of the Company's assets.

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Borrowings, at the Company's election, may be either Base rate or Eurodollar rate loans. Base rate loans bear interest at the prime rate as published from time to time, plus up to 0.75% per annum depending on the Company's debt service coverage ratios. Eurodollar rate loans bear interest at the Eurodollar rate plus up to 3.0% per annum likewise depending on the Company's debt service coverage ratios.

As of September 30, 2004, the Company had outstanding \$10,500,000 under the credit facility, \$2,000,000 of which is classified as short term, \$5,500,000 of which is classified as long term, and an aggregate of \$3,000,000 under letters of credit.

The credit facility includes certain financial covenants, including a covenant measuring: (1) the ratio of the Company's funded indebtedness to earnings before income, taxes, depreciation and amortization, or EBITDA, (2) the ratio of the Company's funded indebtedness to capitalization, and (3) the Company's fixed charges coverage ratio. As of September 30, 2004, the Company was in compliance with these financial covenants.

On August 12, 2004, the Company and the senior lender amended the credit facility. Among other things, the amendment added two additional covenants that required the Company to achieve: (1) minimum stockholders' equity of \$82,878,000 as of October 31, 2004, an increase of \$10,000,000 from the stockholder's equity reflected on the balance sheet as of June 30, 2004, and (2) pro forma 2004 EBITDA (giving effect to the acquisition of CHD Meridian Healthcare as though the transaction had occurred on January 1, 2004) of \$3,560,000. The credit facility amendment also limited the amount the Company could borrow under the facility through October 31, 2004 to \$8,500,000, although the amount of the revolving credit commitments under the facility remained at \$14,000,000.

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I-TRAX, INC. AND SUBSIDIARIES NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

NOTE 6--LONG TERM DEBT (continued)

On October 27, 2004, the Company amended its credit facility with its senior secured lender. The amendment: (1) increased the funded indebtedness to EBITDA ratio and the fixed charge coverage ratio; (2) moved the first measurement date for the consolidated net worth covenant to December 31, 2005, and restated the covenant as a maintenance of minimum stockholders' equity at 90% of the level as of December 31, 2005; (3) excluded the outstanding letters of credit from the credit facility borrowing base through January 1, 2006; and (4) converted amounts outstanding under the term loan commitment of the credit facility into the revolving credit commitment, and eliminated the term loan commitment. The Company continues to have access to \$14,000,000 under the credit facility, of which \$3,000,000 is currently allocated to outstanding letters of credit and up to \$11,000,000 is available under the revolving portion.

NOTE 7--COMMITMENTS AND CONTINGENCIES

Litigation

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CHD Meridian is a defendant in a lawsuit seeking a return of approximately \$556,000 in payments received in the ordinary course of business from a client that filed for protection under bankruptcy laws during 2003. Management believes that such amounts were not preference payments, and as such are not subject to repayment. The outcome of this lawsuit, however, cannot be determined. During the three months ended September 30, 2004, a second lawsuit seeking a return of approximately \$475,000 as preference payments was settled for substantially less than the demand amount.

CHD Meridian is also involved in certain legal actions and claims on a variety of matters related to the normal course of business. Management believes that such legal actions will not have a material effect on the results of operations or the financial position of the Company. (See also Note 9 - Risk Retention Group.)

Compliance with Healthcare Regulations

Because the Company operates in the healthcare industry, it is subject to numerous laws and regulations of Federal, state, and local governments. These laws and regulations include, but are not limited to, matters regarding licensure, accreditation, government healthcare program participation requirements, reimbursement for patient services, and Medicare and Medicaid fraud and abuse. Recently, government activity has increased with respect to investigations and allegations concerning possible violations of fraud and abuse statutes and regulations by healthcare providers. Violations of these laws and regulations could result in, among other things, expulsion from government healthcare programs together with the imposition of significant fines and penalties, as well as significant repayments for patient services previously billed.

Management believes that the Company is in compliance with fraud and abuse statutes as well as other applicable government laws and regulations. Compliance with such laws and regulations can be subject to future government review and interpretation as well as regulatory actions unknown or unasserted at this time.

Significant Customers

As of September 30, 2004, one customer represented 15% of the Company's accounts receivable as reflected on the Company's consolidated balance sheet.

For the three and nine months ended September 30, 2004, one customer of the Company accounted for 12% of the Company's revenue as reflected on the Company's condensed consolidated statement of operations.

I-TRAX, INC. AND SUBSIDIARIES NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

NOTE 7--COMMITMENTS AND CONTINGENCIES (continued)

Risk-Sharing Contracts

From time to time the Company enters into risk-sharing contracts. A risk-sharing contract generally requires the Company to manage the health and wellness of a

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predetermined set of individuals for a term of three to five years. A risk-sharing contract provides that the Company is required to refund to its client a percentage of the Company's fees if its program does not save the client an agreed upon percentage of the client's healthcare costs. The Company did not generate material risk revenue, which may be subject to a refund, during the quarter or nine months ended September 30, 2004.

NOTE 8--STOCKHOLDERS' EQUITY

Preferred Stock

The Company has 2,000,000 authorized shares of preferred stock. As of September 30, 2004, the Company had issued and outstanding 1,200,000 shares of Series A Convertible Preferred Stock. Each share of Series A Convertible Preferred Stock is convertible, at any time, into 10 shares of common stock, has a liquidation preference of \$25.00 per share, the original purchase price, and accrues dividends on that amount at a rate of 8% per year. Dividends are payable, at the Company's option, in cash or common stock, and only upon the Company's liquidation or conversion of the Series A Convertible Preferred Stock into common stock. For the nine months ended September 30, 2004, the Company recorded approximately \$1,282,000 in accrued dividends.

The placement agents that assisted the Company in the sale of 1,000,000 shares of the Series A Convertible Preferred Stock to fund the acquisition of CHD Meridian received a commission of \$1,490,000, and warrants to acquire 492,000 shares of common stock exercisable at \$2.50 per share. Such warrants were valued at \$1,506,000 utilizing the Black-Scholes valuation model. The amount of the cash paid and the value of the warrants have been classified as a cost of equity in the condensed consolidated statement of stockholders' equity.

Common Stock

The Company has 100,000,000 authorized shares of common stock. As of September 30, 2004, the Company had issued and outstanding 24,796,671 shares, which excludes 3,859,200 shares held in escrow for purposes of the CHD Meridian merger earn out.

Warrants

Under the terms of a private placement completed during October 2003, the Company filed a registration statement under the Securities Act of 1933, as amended, covering the resale of the common stock and the common stock underlying warrants issued in the private placement. The Securities and Exchange Commission declared the registration statement effective on February 17, 2004.

In accordance with EITF Issue No. 00-19, "Accounting for Derivative Financial Instruments Indexed To, and Potentially Settled In a Company's Own Stock," upon issuance of such warrants, the Company recorded a liability in the amount of \$2,459,000, representing the fair value of the warrants to acquire 890,000 shares of common stock. The fair value of the warrants was estimated using the Black-Scholes valuation model with the following assumptions: no dividends; risk-free interest rate of 4%; the contractual life of 5 years; and volatility of 112%. The fair value of the warrants was estimated to be \$2,760,000 and \$3,110,000 at December 31, 2003 and February 17, 2004, respectively. The Company recorded an additional liability, with a corresponding charge to operations, of \$301,000 and \$350,000 on December 31, 2003 and February 17, 2004, respectively, associated with the increase in fair value of the warrants.

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I-TRAX, INC. AND SUBSIDIARIES NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

NOTE 8--STOCKHOLDERS' EQUITY (continued)

Warrants (continued)

The adjustments required by EITF Issue No. 00-19 were triggered by the terms of the private placement subscription agreement, which imposed penalties if the Company did not timely register the common stock underlying the warrants issued in the private placement. The Securities and Exchange Commission declared the related registration statement effective within the contractual deadline and the Company incurred no penalties. The adjustments for EITF Issue No. 00-19 had no impact on the Company's working capital, liquidity or business operations.

The warrants were accounted for as a liability, with an offsetting reduction to additional paid-in capital received in the private placement. The warrant liability has been reclassified to equity as of February 17, 2004, the effective date of the registration statement, evidencing the non-impact of these adjustments on the Company's financial position and business operations.

The following table summarizes the Company's activity as it relates to its warrants for the nine months ended September 30, 2004:

	Shares Underlying Warrants
Balance outstanding at January 1, 2004	3,351,372
Quarter ended March 31, 2004:	
Granted	492,000
Exercised	(179,278)
	3,664,094
Balance outstanding at March 31, 2004	3,664,094
Quarter ended June 30, 2004:	
Granted	--
Exercised	(7,500)
	3,656,594
Balance outstanding at June 30, 2004	3,656,594
Granted	--
Exercised	(361,700)
	3,294,894
Balance outstanding at September 30, 2004	

Warrants issued during the nine months ended September 30, 2004 are exercisable at \$2.50 per share. Such warrants were valued at \$1,506,000 and recorded as a cost of equity because they were granted to placement agents in connection with sales of convertible preferred stock.

On October 27, 2004, in connection with the amendment of the Company's senior credit facility (see Note 6 - Long-Term Debt), the Company issued a warrant to purchase 100,000 shares of the Company's common stock at an exercise price of

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\$.01 per share to its senior secured creditor. The warrant expires on December 31, 2014.

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I-TRAX, INC. AND SUBSIDIARIES
 NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
 (UNAUDITED)

NOTE 8--STOCKHOLDERS' EQUITY (continued)

Stock Options

The table below summarizes the activity in the Company's stock option plans for the nine months ended September 30, 2004:

	Incentive Options	Non-Qualified Options	Non-Plan Non-Qualified Options
Outstanding as of January 1, 2004	652,941	795,973	669,000
Granted	70,921	--	--
Exercised	--	--	--
Forfeited/Expired	--	(30,000)	--
Outstanding as of March 31, 2004	723,862	765,973	669,000
Granted	--	--	--
Exercised	--	--	--
Forfeited/Expired	(95,875)	--	--
Outstanding as of June 30, 2004	627,987	765,973	669,000
Granted	--	--	--
Exercised	--	--	--
Forfeited/Expired	(14,291)	--	(175,002)
Outstanding as of September 30, 2004	613,696	765,973	493,998
Vesting Dates:			
December 31, 2004	10,530	31,083	6,666
December 31, 2005	102,448	82,665	26,668
December 31, 2006	54,175	50,004	--
December 31, 2007	5,191	--	--
December 31, 2008	--	--	20,000

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Thereafter

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As of September 30, 2004, exercisable plan and non-plan options to purchase an aggregate of 1,410,307 shares, with exercise prices ranging from \$.005 to \$10.00, were outstanding.

The Company accounts for its employee incentive stock option plans using the intrinsic value method in accordance with the recognition and measurement principles of Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees," as permitted by SFAS No. 123. The adoption of the disclosure requirements of SFAS No. 148 did not have a material effect on the Company's financial position or results of operations.

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I-TRAX, INC. AND SUBSIDIARIES
 NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
 (UNAUDITED)

NOTE 8--STOCKHOLDERS' EQUITY (continued)

Had the Company determined compensation expense based on the fair value at the grant dates for those awards consistent with the method of SFAS 123, the Company's net loss per share would have been increased to the following pro forma amounts:

	For the three months ended September 30, 2004	For the three months ended September 30, 2003	For the nine months ended September 30, 2004
	-----	-----	-----
Net loss as reported	\$ (835,000)	\$ (1,610,000)	\$ (4,455,000)
Add back intrinsic value of the options issued to employee and charged to operations	-	-	-
Deduct stock based employee compensation expense determined under fair value based methods for all awards	(160,000)	(817,000)	(578,000)
	-----	-----	-----

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Pro forma net loss	\$ (995,000)	\$ (2,427,000)	\$ (5,033,000)
	=====	=====	=====
Basic and diluted net loss per share as reported	\$ (0.06)	\$ (0.14)	\$ (1.00)
	=====	=====	=====
Pro forma basic and diluted net loss per share	\$ (0.06)	\$ (0.22)	\$ (1.02)
	=====	=====	=====

The above pro forma disclosure may not be representative of the effects on reported net operations for future years as options vest over several years and the Company may continue to grant options to employees.

The fair market value of each option grant is estimated at the date of grant using the Black-Scholes valuation model with the following weighted-average assumptions:

Dividend yield	0.00%
Expected volatility	112%
Risk-free interest rate	4%
Expected life	5 years

Securities and Exchange Commission Registration

Pursuant to the terms of the merger agreement between the Company and CHD Meridian, on April 19, 2004 the Company filed a registration statement under the Securities Act of 1933, as amended, covering the resale of (1) the common stock issued in the merger, (2) the common stock underlying the convertible preferred stock issued in the merger and the related financing, and (3) the common stock issuable upon exercise of warrants issued to the placement agents in connection with the merger.

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I-TRAX, INC. AND SUBSIDIARIES NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

NOTE 9--Risk Retention Group

During the first quarter of 2004, CHD Meridian formed Green Hills Insurance, a Risk Retention Group (the "RRG"), licensed in the State of Vermont for the purposes of self-insuring a portion of the merged companies' professional and general liability insurance.

The RRG was capitalized with \$2,000,000 in cash and a \$1,000,000 letter of credit under the Company's credit facility. The RRG began issuing policies on a claims-made basis to CHD Meridian LLC, its direct subsidiaries and Physician Groups in May 2004. As of September 30, 2004, cash held by the RRG, which includes \$2,000,000 contributed to RRG's capital, is invested in cash

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equivalents in accordance with the regulations promulgated by the State of Vermont and is reflected on the balance sheet as cash and cash equivalents.

Loss and loss adjustment expense reserves are recorded monthly and represent management's best estimate of the ultimate net cost of all reported and unreported losses incurred from May 1, 2004 through September 30, 2004. Management's estimates are based on an independent actuarial report. The Company does not discount loss and loss adjustment expense reserves. The reserves for unpaid losses and loss adjustment expenses are estimated using individual case-basis valuations and statistical analyses. Those estimates are subject to the effects of trends in severity and frequency. Although considerable variability is inherent in such estimates, management believes the reserves for losses and loss adjustment expenses are adequate. The estimates are reviewed and adjusted continuously as experience develops or new information becomes known; such adjustments are included in current operations. No claims have been filed against these policies as of September 30, 2004. To the extent claims are made against the policies in the future, the Company expects such claims to be resolved within five years of original date of claim.

The RRG does not plan to pay dividends to the policyholders in the foreseeable future.

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PART II. OTHER INFORMATION

Item 6. Exhibits

- 31.1 Certification Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 31.2 Certification Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 32.1 Certification Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
- 32.2 Certification Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

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SIGNATURE

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

I-TRAX, INC.

Date: December 15, 2004

By: /s/ Frank A. Martin

Name: Frank A. Martin

Title: Chief Executive Officer