MEDIFAST INC
Form 10KSB/A
May 31, 2005

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, DC 20549

FORM 10-KSB/A

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

For the fiscal year ended December 31, 2004

Commission File No. 000-23016

MEDIFAST, INC.

DELAWARE	13-3714405
Incorporation State	Tax Identification number
11445 CRONHILL DRIVE, OWINGS MILLS, MD	21117
Principal Office Address	

Phone (410) 581-8042

SECURITIES REGISTERED PURSUANT TO SECTION 12(B) OF THE ACT: NONE

SECURITIES REGISTERED PURSUANT TO SECTION 12(G) OF THE ACT:

COMMON STOCK, PAR VALUE $.001 PER SHARE

Check 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 past 12 months, and (2) has been subject to such filing requirements for the past 90 days.

Yes _X_ No ___

Check if disclosure of delinquent filers pursuant to Item 405 of Regulation S-B 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 or any amendment to this Form 10-KSB.

[ ]

The issuer's revenues for the fiscal year ended December 31, 2004 were $27,340,000

Aggregate market value of voting stock held by non-affiliates of registrant (deemed by registrant for this purpose to be neither a director nor a person known to registrant to beneficially own, exclusive of shares subject to outstanding options, less than 5% of the outstanding shares of registrant's Common Stock) computed by reference to the closing sales price as reported on the American Stock Exchange on December 31, 2004: $3.52.

Number of shares outstanding of registrant's Common Stock, as of December 31, 2004: 11,001,070 shares

Documents incorporated by reference: None

Transitional Small Business Disclosure Format (check one)

Yes ___ No _X_

EXPLANATORY NOTE

This Form 10-KSB/A is being filed for the purpose of adding to or clarifying disclosures to our Controls and Procedures, Significant Accounting Policies, and footnotes previously included in our Form 10-KSB for the fiscal year-ended December 31, 2004. The addition to our Controls and Procedures includes a report on management's internal control over financial reporting required by Item 308(c) of Regulation SB. With respect to our Significant Accounting Policies, we have added greater detail about our revenue recognition policy. The Trademark footnote has been revised to clarify and supplement disclosures that might be useful to the readers of our financial statements. In addition, we have added updated certifications at Exhibits 31.1, 31.2 & 32.1 to conform to Item 601(b)(31) and (32) of Regulation SB.

Except as described above we have not amended or modified the financial information or other disclosures on Form 10-KSB as originally filed. This Form 10-KSB/A does not reflect events occurring after the filing of the original Form 10-KSB, nor does it modify or update the disclosures therein in any way other than as required to reflect the amendments described above and set forth below.

2

PART I

ITEM 1. BUSINESS.

SUMMARY

Medifast, Inc. (the "Company", or "Medifast") is a Delaware corporation, incorporated in 1980. The Company's operations are primarily conducted through five of its wholly owned subsidiaries, Jason Pharmaceuticals, Inc. ("Jason"), Take Shape for Life, Inc. ("TSFL"), Jason Enterprises, Inc., Jason Properties, LLC and Seven Crondall, LLC. The Company is engaged in the production, distribution, and sale of weight management and disease management products and other consumable health and diet products. Medifast, Inc.'s product lines include weight and disease management, meal replacement and sports nutrition products manufactured in a modern, FDA approved facility in Owings Mills, Maryland.

MARKETS

Over the past 20 years the obesity rates in the United States have increases dramatically. The Centers for Disease Control (CDC) estimate that 64% of the U.S. adult population is overweight or obese. The amount of overweight adolescents and children ages 6-19 years have more than tripled since 1980. Currently, the CDC estimates that over 30% of adolescents and children are overweight.

The CDC estimates that in the U.S. the associated costs with overweight and obesity reached $117 billion in 2000. The most common health problems associated with obesity are type II diabetes, coronary heart disease, hypertension and stroke, depression and certain forms of cancer. It's also estimated that poor nutrition and physical inactivity account for more than 300,000 premature deaths per year in the U.S.

A 2003 market research study concluded consumers spend about $39 billion per year trying to lose weight or prevent weight gain. This includes consumer spending on diet foods, medically supervised and commercial weight loss programs, diet books, appetite suppressants, fitness clubs, diet sodas, and videos and cassettes.

DISTRIBUTION CHANNELS

THE MEDIFAST LIFESTYLES PROGRAM- The Medifast Lifestyles Program is a medically supported network of health care professionals who support patients on the Medifast program. Patients order products directly from Medifast's website or toll-free number. The Lifestyles medical practitioner ensures that each patient receives personalized attention throughout the weight loss program. Management estimates that more than 15,000 physicians nationwide have prescribed Medifast as a treatment for their overweight patients since 1980, and an estimated 1 million patients have used its' products to lose and maintain their weight.

The Company maintains an in-house Lifestyles support program for customers who have a Medifast physician, who does not have the time to provide counseling support. These in-house qualified medical practitioners coordinate supervision of the Medifast program with the patient's primary care physician. Customers have access to qualified medical practitioners for program support and advice by calling a toll free telephone help line or by e-mail. The in-house medical and marketing staff have developed extensive program support materials on Medifast products and programs, which are placed free of charge in customer orders, in addition to being available on the Company's website.

TAKE SHAPE FOR LIFE(TM) - The Take Shape for Life program is a comprehensive, medically supervised health network designed to assist in long-term weight loss, health management, or nutritional supplementation. The program features Medifast weight and disease management products, along with a team of personal and professional Health Advisors, to support the individual through their weight and or health management program.

Program entrants are encouraged to consult with their primary care physician and a Take Shape for Life Health Advisor to determine the Medifast program that is right for them. Physician directed Health Advisors are supported, educated and qualified by The Health Institute, a training group staffed by Medifast professionals. Health Advisors obtain Medifast qualification based upon testing of their knowledge on Medifast products and programs.

The Company has developed a Tasting program, which is similar to a home-based Party Plan model for introducing new customers to the Medifast products and program. Physician directed Health Advisors recruit program entrants and provide them with program information, Medifast product samples and the opportunity to order products.

MEDIFAST PHYSICIANS AND CLINICS - Many Medifast physicians have chosen to implement the Medifast program within their practice. These physicians carry an inventory of Medifast products and resell them to patients. They also provide appropriate testing, medical support and evaluations for patients on the program. Physicians can also direct their patients to order directly from Medifast, if they do not have space to stock inventory.

HI-ENERGY WEIGHT CONTROL CENTERS - In 2003, the Company acquired Hi-Energy Weight Control Centers, a national company specializing in weight management programs, with weight loss centers in over 50 locations. During 2004 the number of Hi-Energy Weight Control Centers grew to over 100 nationally. Hi-Energy Weight Control Centers offer a competitive marketing edge through a regional advertising program, exclusive territories and marketing support. The Company continues to seek out qualified licensees to add to its growing number of weight control clinics nationwide. Additionally, the Company is operating 11 corporately owned clinics that serve as models to attract qualified licensees.

CONSUMERS CHOICE SYSTEM(TM) - Founded in March 1996, and acquired by Medifast in 2003, CCS is a retail distribution company focusing on high quality, innovative products for women. CCS products, under the Woman's Wellbeing brand include supplements addressing menopause relief, coronary health and joint health. Products under the UTI brand address the detection, relief and prevention of urinary tract and bladder infections. CCS products are currently distributed in retail outlets nationwide. The Company is currently launching Medifast's "Maintain," a pharmacist-directed Diabetic line of products. The CCS business is supported by a website and toll-free customer service line where customers can inquire about product information and retail availability.

THE MEDIFAST(R) BRAND

Medifast is a medically supervised weight management program, which specializes in multidisciplinary patient education programs using the highest quality meal replacement supplements. In recent years Medifast's core products and programs have continued to expand over a wellness spectrum to include disease management products. Medifast offers products specially formulated for Diabetics as well as products for women's health, joint health and coronary health.

4

In 2003, Medifast began a two-year study with The Johns Hopkins Bloomberg School of Public Health to evaluate the efficacy of its Medifast Plus for Diabetics compared to basic nutrition recommendations by the American Diabetes Association (ADA). Preliminary results showed that participants using Medifast Plus for Diabetics lost twice as much weight as those following the ADA's guidelines. Additionally, two-thirds of those on the Medifast program lost at least 5% of their weight, which is a standard measure of the Food and Drug Administration's (FDA) threshold to indicate clinically significant weight loss, versus one-quarter of those on the ADA diet. In addition to weight loss, the initial study results indicate that Medifast participants sustained an average 9% decrease in blood fasting glucose and an average 19% decrease in insulin levels. The final study results are expected to be released in 2005.

Many Medifast Plus for Diabetics products have earned the coveted Seal of Approval from the Glycemic Research Institute. The line, designated as Low Glycemic, does not overly stimulate blood glucose and insulin and does not stimulate fat-storing enzymes. Products included in the Medifast Plus for Diabetics line consist of three delicious patented shakes, home style chili, apple cinnamon, French vanilla berry oatmeal, maple and brown sugar oatmeal, creamy chicken soup, creamy broccoli soup, chicken noodle soup, minestrone soup and two snack bars.

The Company expanded the product line of its cutting edge adolescent weight management program, Fit!(TM) in 2003. The line, which formerly consisted of only one ready-to-drink and two chocolate bars, now consists of three delicious powdered shakes, vanilla berry oatmeal, chicken noodle soup, hot cocoa with marshmallows, chocolate pudding, 3 power-packed bars and one ready-to-drink.

Medifast has commissioned another study at Johns Hopkins that began in 2004 to evaluate the effectiveness of Medifast Fit! meal replacements in a weight loss program for overweight children. The study aims to prove that the Medifast program will generate greater initial weight loss, greater reductions in body fat and greater improvements in overall health than a standard reference diet. The study will also evaluate the weight loss outcomes in a joint parent-child approach versus children dieting without parental support.

Most Medifast(R) products qualify to make the FDA's heart healthy claim, "May Reduce the Risk of Heart Disease." In order to make this claim, a product must contain at least 6.25 grams of soy protein per serving and be low in fat, saturated fat, and cholesterol. Unlike popular fad diets and herbal supplements, Medifast(R) products are a safe, nutritionally balanced choice, offering gender specific formulas containing high protein and low carbohydrates, a soy protein source rather than animal protein source, and vitamin and mineral fortification. It is very difficult to meet the minimum recommended nutritional requirements on a low-calorie diet, but a dieter can easily meet these requirements using the nutrient dense Medifast(R) brand of meal replacement food supplements.

Medically supervised, low calorie diets are continuing to gain popularity, as consumers search for a safe and effective solution that provides balanced nutrition, quick weight loss and valuable behavior modification education. In addition, consumers are becoming more aware of chronic diseases such as diabetes and coronary health.

COMPETITION

There are many different kinds of diet products and programs within the weight loss industry. These include a wide variety of commercial weight loss programs, pharmaceutical products, weight loss books, self-help diets, dietary supplements, appetite suppressants and meal replacement shakes and bars.

5

The Company has proven it can compete in this competitive market because its products have been clinically tested and proven at Johns Hopkins University and have been safely and effectively used by customers for over 20 years. Medifast has been on the cutting edge of product development with soy based nutritional and weight management products since 1989. These products are formulated with high-quality, low-calorie, low-fat ingredients that provide alternatives to fad diets or medicinal weight loss remedies.

PRODUCTS

The Company offers a variety of weight and disease management products under the Medifast(R) brand and for select private label customers. The Medifast(R) line includes Medifast(R) 55, Medifast(R) 70, Medifast(R) Plus for Appetite Suppression, Medifast(R) Plus for Diabetics, Medifast(R) Plus for Joint Health, Medifast(R) Plus for Women's Health, Medifast(R) Plus for Coronary Health, Medifast(R) Fit!, Medifast(R) Take ShapeTM, Medifast(R) Supplement Bars, Medifast(R) Creamy Soups, Medifast(R) Minestrone Soup, Medifast(R) Hot Cocoa, Medifast(R) Oatmeals, Medifast(R) Pro Teas, Medifast(R) Chicken Noodle Soup, Medifast(R) Fast Soups, Medifast(R) Homestyle Chili and Medifast(R) Multigrain Crackers.

Medifast nutritional products are formulated with high-quality, low-calorie, low-fat ingredients. Many Medifast products are soy based and contain 24 vitamins and minerals, as well as other nutrients essential for good health. The Company uses DuPont Protein Technologies' Supro(R) brand soy protein, which is a high-quality complete protein derived from soybeans.

The Consumers Choice Systems subsidiary sells products under the private label Woman's Wellbeing. These products include Menopause Relief Pills, Personal Cream Lubricant, a UTI Home Screening Test Stick, UTI Cleansing Wipes, UTI Cranberry-Plus-Blueberry, Women's Wellbeing Meal Replacements and all-natural weight loss pills.

Medifast(R) brand awareness continues to expand through product development, line extensions, and the Company's emphasis on quality customer service, technical support and publications developed by the Company's marketing staff. Medifast(R) products have been proven to be effective for weight and disease management in clinical studies conducted by the U.S. government and Johns Hopkins University. The Company has continued to develop its sales and marketing operations with qualified management and innovative programs. The Company's facility in Owings Mills, MD manufactures powders and supplement bars and subcontracts the production of its Ready-to-Drink products.

NEW PRODUCTS

The Company expanded the Medifast product line with twenty-three new products in 2004. Medifast introduced Medifast(R) Cappuccino, Medifast(R) Chai Latte, Medifast(R) Hot Cocoa with Marshmallows, Medifast(R) Maple and Brown Sugar Oatmeal, Medifast(R) Banana Cream Pudding, Medifast(R) Chicken and Wild Rice Soup, Medifast(R) Cranberry Mango Fruit Drink, Medifast(R) Tropical Fruit Punch Drink and Medifast(R) Garden Vegetable Crackers. Medifast also introduced a line of salad dressings and three new meal replacement bars. Last, the Company introduced a line called Essential 1 Meals that includes grilled chicken breasts, grilled beef patties, tuna salad and chicken salad.

Consumers Choice Systems reformulated its existing Menopause Relief capsules, adding a new type of soy and developing the product into an extended time-release formula, branded as Menopause Relief 24. Menopause Relief 24 is the only time release formula for relieving the symptoms of menopause in the market today. The Company also introduced two new all natural weight loss pills in 2004

under the private label Woman's Wellbeing called Active Trim and Always Trim. These two new diet formulas are all-natural capsules that help burn fat, boost energy and suppress appetite.

MARKETING

The Company continued to build and leverage its core Medifast brand through multiple marketing strategies to its target audiences. Print advertising, television, and radio were all used to target new customers by stressing Medifast's quick, easy and safe approach to weight management. Also, direct mail has been utilized to encourage and support existing customers.

Online advertising began to be used in 2004 and it included keyword search, banner ads, affiliate programs, and targeted direct email campaigns. The online advertising has been supported by Medifast's well designed, user-friendly website, which provides a wealth of information and customer support for easy ordering functionality.

The Company has expanded its public relations efforts in order to gain exposure in the media to promote greater consumer awareness of the Medifast brand. Mr. Dick Vitale, the famous basketball commentator, continues to be the Company's spokesperson, particularly supporting the Company's Take Shape for Life programs and its Diabetic products and programs.

SALES

The Company's Sales division handles three primary areas:

Physician and Clinic Sales-- The sales team is responsible for prospecting larger medical accounts, clinics, hospitals, and HMOs. During 2004, the sales team attended a number of medical professional trade shows, which expanded Medifast's penetration of the clinical business segment.

Hi-Energy Weight Control Centers-- During 2004 Hi-Energy provided ongoing support to its licensees as well as to the Company's 11 corporately owned centers which opened at the end of 2004. This support included marketing materials, ads, on-site trainings, fitness programs, nutritional programs and clinical operation materials and forms. Employees attended professional trade shows, prospected new licensees, and partnered with area physicians to provide Hi-Energy programs and services to local hospitals and private practices.

Take Shape for Life-- Provides a sales force of Health Advisors who support patients and their primary care physicians with a defined support program.

MANUFACTURING

Jason Pharmaceuticals, Inc., the Company's wholly owned manufacturing subsidiary, produces over 95% of the Medifast products in a state-of-the-art food and pharmaceutical-grade facility in Owings Mills, Maryland. Management purchased the plant in July 2002 for $3.4 million. The Company purchased additional lines for the internal production of its growing nutritional meal replacement bar product line in 2003.

The manufacturing facility has the capacity for significant increases to its production output with minimal capital expenditures. It is presently operating on a single shift. Adding an additional shift, along with diminutive

machinery expenses would enable the Company to produce enough products to generate over $200 million in sales.

Manufacturing processes, product labeling, quality control and equipment are subject to regulations and inspections mandated by the Food & Drug Administration (FDA), the Maryland State Department of Health and Hygiene, and the Baltimore County Department of Health. The plant strictly adheres to all GMP practices and has maintained its status as an "OU" (Orthodox Union)

Kosher-approved facility since 1982.

FINANCING AND STRATEGIC ALTERNATIVES

Management desires to develop strategic marketing relationships with other third parties having existing relationships with the medical professional community, specifically to reach the diabetic population in the United States and to secure international distribution in Europe and Asia.

GOVERNMENTAL REGULATION HISTORY

The formulation, processing, packaging, labeling and advertising of the Company's products are subject to regulation by several federal agencies, but principally by the Food and Drug Administration (the "FDA"). The Company must comply with the standards, labeling and packaging requirements imposed by the FDA for the marketing and sale of medical foods, vitamins, and nutritional products. Applicable regulations prevent the Company from representing in its literature and labeling that its products produce or create medicinal effects or possess drug-related characteristics. The FDA could, in certain circumstances, require the reformulation of certain products to meet new standards, require the recall or discontinuation of certain products not capable of reformulation, or require additional record keeping, expanded documentation of the properties of certain products, expanded or different labeling, and scientific substantiation. If the FDA believes the products are unapproved drugs or food additives, the FDA may initiate similar enforcement proceedings. Any or all such requirements could adversely affect the Company's operations and its financial condition.

The FDA also requires "medical food" labeling to list the name and quantity of each ingredient and identify the product as a "weight management/modified fasting or fasting supplement" in the labeling.

To the extent that sales of vitamins, diet, or nutritional supplements may constitute improper trade practices or endanger the safety of consumers, the operations of the Company may also be subject to the regulations and enforcement powers of the Federal Trade Commission ("FTC"), and the Consumer Product Safety Commission. The Company's activities are also regulated by various agencies of the states and localities in which the Company's products are sold. The Company's products are manufactured and packaged in accordance with customers' specifications and sold under their private labels both domestically and in foreign countries through independent distribution channels.

PRODUCT LIABILITY AND INSURANCE

The Company, like other producers and distributors of ingested products, faces an inherent risk of exposure to product liability claims in the event that, among other things, the use of its products results in injury. The Company maintains insurance against product liability claims with respect to the products it manufactures. With respect to the retail and direct marketing

distribution of products produced by others, the Company's principal form of insurance consists of arrangements with each of its suppliers of those products to name the Company as beneficiary on each of such vendor's product liability insurance policies. The Company does not buy products from suppliers who do not maintain such coverage.

EMPLOYEES

At December 31, 2004, the Company employed 130 full-time and contracted employees, of whom 46 were engaged in manufacturing, warehouse management, and shipping, and 84 in marketing, administrative, call center and corporate support functions. None of the employees are subject to a collective bargaining agreement with the Company.

ITEM 2. DESCRIPTION OF PROPERTY

The Company owns a 49,000 square-foot facility in Owings Mills, Maryland, which contains its Corporate Headquarters and manufacturing plant. In 2003, the Company purchased a state-of-the-art 119,000 square-foot distribution facility in Ridgely, Maryland. The facility gives the Company the ability to distribute over $200 million of Medifast product sales per year. In 2004, the Company purchased a 3,000 square foot conference and training facility in Ocean City, Maryland. The facility will be used to conduct corporate training meetings, Board of Director Meetings and employee morale and wellness programs. The Company has 11 leases for its corporately owned Hi-Energy Weight Control clinics throughout Florida, Arkansas, Mississippi and Texas. The leases range in terms from one to five years.

ITEM 3. LEGAL PROCEEDINGS.

On December 16, 2003, John Donavin, on behalf of the General Public, filed suit, against Jason Pharmaceuticals, Inc. in the Superior Court of the State of California, City and County of San Francisco. The suit alleges that Medifast bars contain Vitamin D3 or Vitamin D in violation of Federal laws and regulations, and asks for equitable relief and damages. The Company's General counsel believes that the Company's formulation used in its "meal replacement" bars for over 20 years has been and is in conformity with current and past FDA regulations. The Company believes that the plaintiff's claim lacks merit and may even be considered frivolous. The suit has been stayed upon appeal to the FDA to clarify its regulations. The Company believes recent legislation restricting the ability of plaintiff's lawyers from filing local class action suits should favor the Company's legal position in this case.

A former counsel continues to claim that he transferred his personal Medifast stock to a third party organization in 2000, in an attempt to keep these assets out of his bankrupt estate and therefore outside the jurisdiction of the Bankruptcy Court. The Company contests, and will vigorously defend, all such claims made by him. The Trustee in Bankruptcy for his bankruptcy estate has determined that he has no authority to transfer these shares, and has concluded that the attempted transfer was therefore invalid. The trustee has demanded that he produce the shares, and plans to file a petition with the Bankruptcy Court requesting that the Court order him to do so. These assets will be made a part of the bankrupt estate and will be used to pay creditors.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

The Medifast Annual Shareholder Meeting was held on September 3, 2004 at Sunrise Distributing, the Company's distribution headquarters. The shareholders voted Bradley T. MacDonald (98%) and Rev. Donald F. Reilly, O.S.A.* (98%) as Class I Directors that will hold office until 2007, Scott Zion* (98%) and Michael C. MacDonald (98%) as Class II Directors, and Mary T. Travis* (98%), Michael J. McDevitt (98%), and Rev. Joseph Calderone, O.S.A.* (98%) as Class III Directors. Class II and III Directors will hold office until the next Annual Shareholders Meeting at which time their respective class term expires and their respective successors will be duly elected and qualified. Additionally, the shareholders approved the appointment of Bagell, Josephs & Company, LLC, an independent member of the BDO Seidman Alliance, as the Company's independent auditors for the fiscal year ending December 31, 2004.

Additionally the Board of Directors elected Mr. Bradley T. MacDonald as Chairman of the Board and CEO and Mr. Conrad Sump, Esq. as Secretary of the Corporation.

* Independent Director

PART II

ITEM 5. MARKET FOR COMMON EQUITY AND RELATED STOCKHOLDER MATTERS.

(a) The Company's Common Stock has been quoted under the symbol MED since December 20, 2002. The old symbol, MDFT, had been traded since February 5, 2001. The common stock is traded on the American Stock Exchange. The following is a list of the low and high closing prices by fiscal quarters for 2004 and 2003:

	2004	
	Low	High
Quarter ended March 31, 2004	8.60	14.05
Quarter ended June 30, 2004	4.78	9.33
Quarter ended September 30, 2004	3.05	5.09
Quarter ended December 31, 2004	3.20	5.24

	2003	
	Low	High
Quarter ended March 31, 2003	3.79	6.10
Quarter ended June 30, 2003	4.80	14.95
Quarter ended September 30, 2003	11.15	17.21
Quarter ended December 31, 2003	11.60	18.49

(b) The quotations reflect inter-dealer prices, without retail mark-up, markdown or commissions and may not represent actual transactions.

(c) There were 6,366 record holders of the Company's Common Stock, as of December 31, 2004. The Company had 6 preferred holders of the Company's stock as of December 31, 2004.

(d) No dividends on common stock were declared by the Company during 2004 or 2003.

ITEM 6. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS.

FORWARD LOOKING STATEMENTS

This document contains forward-looking statements which may involve known and unknown risks, uncertainties and other factors that may cause Medifast, Inc. actual results and performance in future periods to be materially different from any future results or performance suggested by these statements. Medifast, Inc. cautions investors not to place undue reliance on forward-looking statements, which speak only to management's expectations on this date.

2004 COMPARISON WITH 2003

OPERATING

Consolidated net sales for 2004 were $27,340,000 as compared to 2003 sales of $25,379,000, an increase of $1,961,000, or 8%. A major reason for the revenue increase for the Company is attributed to the continued success from the Take Shape for Life division, national advertising, the Hi-Energy acquisition and the redesigned website. The Take Shape for Life division added a Take Shape for Life replicating website option for Health Advisors, an Internet distribution program for their customers, as well as the new Tasting Party Program. These have proven to be effective at generating revenues and recruiting Health Advisors into the Take Shape for Life Network. The national advertising campaign included print, TV, radio, direct mail and web marketing. The Company increased its Internet sales in 2004 as compared to 2003, by redesigning its website and increasing its web marketing. The redesigned website created an easy to use shopping cart and a more user-friendly interface. The acquisition of Hi-Energy Weight Control Centers contributed to revenues throughout 2004.

Cost of sales decreased from $6,825,000 in 2003 compared to $6,746,000 in 2004, a decrease of $79,000. The decrease is attributed to decreases in costs through economies of scale.

Gross margins increased to 75% in 2004 from 73% in 2003. This was largely due to greater economies of scale as a result of the acquisition of the Company's 119,000 square foot distribution facility thereby creating higher margins of the Medifast(R) products through purchasing capabilities. The increase is also attributed to the increased margin of Medifast(R) direct and Internet sales directly to patients via the Lifestyles and Take Shape for Life programs. Selling, general and administrative (SG&A) expenses of $17,590,000 for 2004 were $2,634,000 more than the $14,956,000 in 2003, due to increased advertising expenses to include television advertising, celebrity endorsements, expenses involved with starting and operating new corporately owned Hi-Energy Weight Control Clinic locations, the expansion of the Take Shape for Life commissioned sales organization, and overall corporate infrastructure improvements. The Company experienced income from operations for the year 2004 of $3,004,000. This compares with income from operations of $3,598,000 in 2003, a decrease of 17%.

In 2004, the Company realized a tax expense of $1,159,000, as compared to a tax expense of $1,148,000 in 2003 as a result of the elimination of the deferred tax asset and the net operating loss for income tax purposes. Interest expense increased to $245,000 in 2004, as compared to $154,000 in 2003. This increase was due to a complete year of additional debt, which was acquired in 2003.

A preferred stock dividend in the amount of $18,000 was expensed to shareholders in 2004.

LIQUIDITY AND CAPITAL RESOURCES

At December 31, 2005, the Company had net working capital of $7,465,000, a decrease of $1,933,000 from the $9,398,000 net working capital balance at December 31, 2003. Cash and investment securities at December 31, 2004 were $3,238,000. On November 7, 2003 Medifast, Inc.'s wholly owned subsidiary Jason Pharmaceuticals, Inc. increased its Secured Line of Credit from $1,000,000 to $5,000,000 from Mercantile Safe-Deposit and Trust of Baltimore, Maryland. The line of credit is at LIBOR plus two percent. The increased line may be used to finance equipment, inventory, and receivables of Medifast, Inc. The Company currently has no off-balance sheet arrangements.

In the year ended December 31, 2004, the Company generated a negative cash flow of $2,332,000 from operations, primarily attributable to purchases of inventory and the pay down of accounts payable and accrued expenses.

In the year ended December 31, 2004, net cash used in investing activities was $3,940,000, which primarily consisted of the purchase of intangible assets, purchase of property and equipment, and the purchase of a building.

In the year ended December 31, 2004, net cash used in financing activities was $304,000, representing the principal repayments of long-term debt.

In pursuing its business strategy, the Company may require additional cash for operating and investing activities. The Company expects future cash requirements, if any, to be funded from operating cash flow and cash flow from financing activities.

There are no current plans or discussions in process relating to any material acquisition that is probable in the foreseeable future

On June 11, 2003 Jason Enterprises, Inc. acquired the assets of Consumers Choice Systems, Inc., a Delaware Corporation. The Company obtained all the assets of the business that support their retail and international business including the distribution rights in 18,000 retail food and drug stores. Jason Enterprises, Inc. acquired the assets for 76,120 shares of Medifast, Inc. restricted common stock and 50,000 five-year warrants at a purchase price of $10.00 per share. The transaction will be accounted for as an asset purchase transaction. The Company is expecting to record limited and selected liabilities that amount to approximately $1.35 million.

On July 24, 2003 the Company announced an agreement with Amazon.com. Through the agreement the Consumer Choice Systems, Women's Wellbeing branded products will be offered on Amazon.com's website in the women's health section.

On July 25, 2003, the Company announced that it had sold an aggregate of 550,000 shares of common stock and warrants to purchase 82,500 shares of common stock (the "PIPE Shares") to Mainfield Enterprises, Inc. and Portside Growth & Opportunity Fund. The shares of common stock were sold for a cash consideration of $12.40 per share, or a total of $6,820,000, and the warrants, exercisable for a period of five years from the date of issuance, at an exercise price equal to one hundred fifteen percent (115%) of the five-day volume weighted average price (the "PIPE Transaction"), all pursuant to the terms of that certain Securities Purchase Agreement by and between the Company and Mainfield Enterprises, Inc. and Portside Growth & Opportunity Fund dated as of July 24, 2003 (the "Securities Purchase Agreement").

On September 12, 2003 Medifast, Inc.'s wholly owned subsidiary Seven Crondall, LLC purchased a 119,825 sq. foot distribution facility located at 601 Sunrise Ave., Ridgely, Maryland 21660 from New Roads, Inc. for $2,200,000. The Company financed $1,760,000 through Merrill Lynch Capital at the 30 day LIBOR interest rate plus 220 basis points over seven years.

On November 7, 2003 Medifast, Inc.'s wholly owned subsidiary Jason Properties, LLC purchased the assets of Hi-Energy Weight Control Centers, located in Gulf Breeze, Florida. The acquisition includes equipment, inventory, trademarks, and licenses for fifty Hi-Energy clinics. The clinics are located primarily in the southeastern region of the United States. The assets were purchased for $1,500,000 in cash, which included selected liabilities, capital expenditures, costs of assets and miscellaneous fees.

SEASONALITY

The Company's weight management/diet control is subject to seasonality. Traditionally the holiday season in November/December of each year are considered poor sales for diet control products and services. January and February generally show increases in sales.

INFLATION

To date, inflation has not had a material effect on the Company's business.

INFORMATION SYSTEMS INFRASTRUCTURE

Throughout 2004 the Company significantly enhanced the capacity and the functionality of its IT infrastructure. The enhancements include a more robust email system and upgraded network operating system. The Company also added additional servers, as well as a higher capacity network switch. A Virtual Private Network was implemented between the remote office sites. The Company continued its upgrades and service enhancements to its Navision (ERP) system to more effectively and efficiently manage inventory and sales growth.

ITEM 7. CONTROLS AND PROCEDURES

(a) Evaluation of Disclosure Controls and Procedures

The term "disclosure controls and procedures" is defined in Rules 13a-15(e) and 15d-15(e) of the Securities Exchange Act of 1934, as amended (the "Exchange Act"). This term refers to the controls and procedures of a company that are designed to ensure that information required to be disclosed by a company in the reports that it files under the Exchange Act is recorded, processed, summarized, and reported within the required time periods. Our Chief Executive Officer and our President have evaluated the effectiveness of our disclosure controls and procedures as of the end of the period covered by this annual report. They have concluded that, as of that date, our disclosure controls and procedures were effective at ensuring that required information will be disclosed on a timely basis in our reports filed under the Exchange Act.

(b) Changes in Internal Control over Financial Reporting

No change in our internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) occurred during the period covered by this report that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

CODE OF ETHICS

In September 2002, the Company implemented a Code of Ethics by which directors, officers and employees commit and undertake to personal and corporate growth, dedicate themselves to excellence, integrity and responsiveness to the marketplace, and work together to enhance the value of the Company for the shareholders, vendors, and customers.

TRADING POLICY

In March 2003, the Company implemented a Trading Policy whereby if a director, officer or employee has material non-public information relating to the Company, neither that person nor any related person may buy or sell securities of the Company or engage in any other action to take advantage of, or pass on to others, that information. Additionally, insiders may purchase or sell MED securities if such purchase or sale is made within 30 days after an earnings or special announcement to include the 10-KSB, 10-QSB and 8-K in order to insure that investors have available the same information necessary to make investment decisions as insiders.

ITEM 8. FINANCIAL STATEMENTS.

See pages F-1 through F-20.

ITEM 9. CHANGES AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURES.

There were no disagreements with the Company's independent auditors, regarding accounting and financial disclosures for the fiscal year ending December 31, 2004.

PART III

ITEM 10. DIRECTORS, EXECUTIVE OFFICERS, PROMOTERS AND CONTROL PERSONS; COMPLIANCE WITH SECTION 16(A) OF THE EXCHANGE ACT.

(a) The following are the Board of Directors:

Name	Age	Position	Date First Became Director
Bradley T. MacDonald ..	57	Chairman of the Board, Chief Executive Officer and Director	1996
Donald F. Reilly	57	Director	1998
Michael C. MacDonald ..	51	Director	1998
Scott Zion............	54	Director	1999
Michael J. McDevitt....	56	Director	2002
Mary T. Travis.........	54	Director	2002
Joseph D. Calderone....	56	Director	2003

BRADLEY T. MACDONALD became Chairman of the Board and Chief Executive Officer of Medifast, Inc. on January 28, 1998. Prior to joining the Company, he was appointed as Program Director of the U.S. Olympic Coin Program of the

Atlanta Centennial Olympic Games. Mr. MacDonald was previously employed by the Company as its Chief Executive Officer from September 1996 to August 1997. From 1991 through 1994, Colonel MacDonald returned to active duty to be Deputy Director and Chief Financial Officer of the Retail, Food, Hospitality and Recreation Businesses for the United States Marine Corps. Prior thereto, Mr. MacDonald served as Chief Operating Officer of the Bonneau Sunglass Company, President of Pennsylvania Optical Co., Chairman and CEO of MacDonald and Associates, which had major financial interests in a retail drug, consumer candy, and pilot sunglass companies. Mr. MacDonald was national president of the Marine Corps Reserve Officers Association and retired from the United States Marine Corps Reserve as a Colonel in 1997, after 27 years of service. He has been appointed to the Defense Advisory Board for Employer Support of the Guard and Reserve (ESGR). Mr. MacDonald serves on the Board of Directors of the Wireless Accessories Group (OTCBB: WIRX). He is also on the Board of Directors of the Marine Corps Reserve Toys for Tots Foundation and is a Foundation Trustee of the Marine Reserve Association.

REVEREND DONALD FRANCIS REILLY, O.S.A., a Director, holds a Doctorate in Ministry (Counseling) from New York Theological and an M.A. from Washington Theological Union as well as a B.A. from Villanova University. Reverend Don Reilly was ordained a priest in 1974. His assignments included Associate Pastor, pastor at St. Denis, Havertown, Pennsylvania, Professor at Villanova University, Personnel Director of the Augustinian Province of St. Thomas of Villanova, Provincial Counselor, Founder of SILOAM Ministries where he ministers and

16

counsels HIV/AIDS patients and caregivers. He is currently on the Board of Directors of Villanova University, is President of the board of "Bird Nest" in Philadelphia, Pennsylvania and is Board Member of Prayer Power. Fr. Reilly was recently elected Provincial of the Augustinian Order at Villanova, PA. He oversees more than 300 Augustinian Friars and their service to the Church, teaching at universities and high schools, ministering to parishes, serving as chaplain in the Armed Forces and hospitals, ministering to AIDS victims, and serving missions in Japan and South America.

MICHAEL C. MACDONALD, a Director, is a corporate officer and President of Global Accounts and Marketing Operations, for the Xerox Corporation. Mr. MacDonald's former positions at Xerox Corporation include executive positions in the sales and marketing areas. He is currently on the Board of Trustees of Rutgers University and a Director of the Jimmy V Foundation. Mr. MacDonald is the brother of Bradley T. MacDonald, the CEO of the Company.

SCOTT ZION, is a Director and also Assistant Secretary for Medifast, Inc. He received a Bachelor of Arts Degree from Denison University, Granville, Ohio. Mr. Zion is currently a principal in Resources Development, Inc. a health care consulting company in Napa, California. Prior to forming Resources Development, he was Senior Vice President of Sales and Marketing for Santen, Inc. an ophthalmic pharmaceutical company. Before Santen, he was Senior Vice President and General Manager for Akorn, Inc., an ophthalmic manufacturing and distribution company. Pilkington Barnes Hind, a worldwide contact lens company, as Head of North American Sales and Marketing, also employed him. Prior to that, he spent 20 years with the Mead Johnson Nutritional Division of Bristol Myers Squibb in various positions of increasing responsibility in sales management. He has extensive experience in nutritional products particularly in the areas of sales and marketing.

MICHAEL J. MCDEVITT, a Director, is a retired FBI Special Agent with over 29 years of government service with the United States Marine Corps and the FBI. He had attained Senior Executive status within the FBI's Investigative

Technology Branch and is currently employed within the private sector as a physical security specialist.

MARY T. TRAVIS, a Director, is currently employed with Sunset Mortgage Company, L.P. in Pennsylvania as the Senior Vice President of wholesale operations and was formerly the Vice President of operations for the Financial Mortgage Corporation. Mrs. Travis is an expert in mortgage banking with over 36 years of diversified experience. She is an approved instructor of the Mortgage Bankers Association Accredited School of Mortgage Banking. Mrs. Travis was also formally a delegate and 2nd Vice president of the Mortgage Bankers Association of Greater Philadelphia and the Board of Governors of the State of Pennsylvania. She is the key financial executive on the Company's Audit Committee providing oversight of the Company's external auditors.

REVEREND JOSEPH D. CALDERONE, O.S.A., a Director, is the Associate Director of Campus Ministry at Villanova University. He formerly spent over eight years with the Loyola University Medical Center as the hospital Chaplain and taught multiple courses including Introduction to the Practice of Medicine and Business Ethics. Rev. Calderone is currently a Captain in the US Navy Reserves and serves as the Wing Chaplain for the 4th Marine Aircraft Wing.

17

ITEM 11. EXECUTIVE COMPENSATION.

The following table sets forth information as to the compensation of the Chief Executive Officer of the Company and each other executive officer that received compensation in excess of $100,000 for 2004, 2003, and 2002.

Annual Compensation

Name	Year	Salary ($)	Bonus ($)	Value of Common/ Preferred Stock Issued in Lieu of Cash	Option Awards
Bradley T. MacDonald	2004	225,000	0	0	0
Chairman of the Board	2003	225,000	112,000	0	0
& CEO	2002	145,000	75,000	0	100,000(1)

----

(1) The Board of Directors reinstated 100,000 options at $1.50 per share granted in 1997 and not exercised. Mr. MacDonald exercised those options in December 2002 per the Board's direction.

Annual Compensation

Name	Year	Salary ($)	Bonus ($)	Value of Common/ Preferred Stock Issued in Lieu of Cash	Option Awards
Leo V. Williams, III	2004	118,000	0	0	10,000
Executive Vice President					

18

STOCK OPTIONS

The Company's 1993 Employee Stock Option Plan (the "Plan"), as amended in July 1995, December 1997, June 2002, and again in July 2003 authorizes the issuance of options for 1,250,000 shares of Common Stock. The Plan authorizes the Board of Directors or the Compensation Committee appointed by the Board to grant incentive stock options and non-incentive stock options to officers, key employees, directors, and independent consultants, with directors who are not employees and consultants eligible only to receive non-incentive stock options. Employee stock options are vested over 2 years.

* The following tables set forth pertinent information as of December 31, 2004 with respect to options granted under the Plan since its inception to the persons set forth under the Summary Compensation Table, all current executive officers as a group and all current Directors who are not executive officers as a group of the Company. In addition, a chart listing option holders, grants made in FY 2004, and a list of aggregated options and the value of these options, is provided.

	BRADLEY T. MACDONALD (1)	ALL CURRENT EXECUTIVE AS A GROUP	ALL CURRENT INDEPENDENT AS A GROUP
Options granted........................	215,000	75,000	110,000
Average exercise price.................	$ 0.86	$ 1.98	$ 1.07
Options exercised......................	215,000	49,999	100,000
Average exercise price.................	$ 0.86	$ 0.88	$ 0.70
Shares sold............................	*	*	*
Options unexercised as of 12/31/04......	0	11,667	10,000

	FY 04 Grants @ Price & Expiration Month/Year	Approximate 5 YR Potential Realizable Value at 10% Annual Stock Appreciation	Unexercised Options as of 12/31/04	V Une O as o
Current Executive Officers and Directors	10,000 @ $8.60 2009	$13.86	10,000	
Employees	20,000 @ $8.60 2009	$13.86	20,000	
Consultants	0		0	
			30,000	

19

NUTRACEUTICAL GROUP INDUSTRY COMPARISON OF STOCK PRICES

Company	December 31, 2004 Stock Price	December 31, 2003 Stock Price	$ Change

Medifast (MED)..................................	$ 3.52	$14.10	10.58
Natural Alternatives International, Inc. (NAII)....	9.23	6.40	2.83
Weider Nutrition (WNI)............................	4.35	4.45	(0.10)
Pure World, Inc (PURW)............................	1.56	2.51	(0.95)
Natures Sunshine Products, Inc. (NATR)............	20.36	8.31	12.05

Company	December 31, 2004 Stock Price	December 31, 1999 Stock Price	$ Change
Medifast (MED)..................................	$ 3.52	$ .22	3.30
Natural Alternatives International, Inc. (NAII)....	9.23	3.25	5.98
Weider Nutrition (WNI)............................	4.35	3.22	1.13
Pure World, Inc (PURW)............................	1.56	3.13	(1.57)
Natures Sunshine Products, Inc. (NATR)............	20.36	7.42	12.94

INDEX COMPARISON

$100 invested in 1999 would return:

	1999	2004
Nutraceutical Group Index......................	$ 100	$ 469
Medifast......................................	$ 100	$ 1600

Factual material is obtained from sources believed to be reliable, but the publisher is not responsible for any errors or omissions contained herein.

COMPENSATION OF DIRECTORS

The Company is authorized to pay a fee of $300 for each meeting attended by its Directors who are not executive officers. It reimburses those who are not employees of the Company for their expenses incurred in attending meetings. Independent Directors claimed $17,500 in Director's fees and/or expenses in 2004. See "Executive Compensation - Stock Options" for stock options granted under the 1993 Plan to the Directors.

20

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT.

The following table sets forth information with respect to the beneficial ownership of shares of Common Stock or voting Preferred Stock as of December 31, 2004 of the Chief Executive Officer, each Director, each nominee for Director, each current executive officer named in the Summary Compensation Table under "Executive Compensation" and all executive officers and Directors as a group. The number of shares beneficially owned is determined under the rules of the Securities and Exchange Commission and the information is not necessarily indicative of beneficial ownership for any other person. Under such rules, "beneficial ownership" includes shares as to which the undersigned has sole or shared voting power or investment power and shares, which the undersigned has the right to acquire within 60 days of March 15, 2005 through the exercise of any stock option or other right. Unless otherwise indicated, the named person has sole investment and voting power with respect to the shares set forth in the table.

NAME AND ADDRESS*	NUMBER OF SHARES	% OF OUTSTANDING
Bradley T. MacDonald	1,270,373(1)	11.6%
Donald F. Reilly....................	65,452	0.6%
Michael C. MacDonald................	39,354	0.4%
Scott Zion..........................	192,000	1.8%
Mary Travis.........................	5,340	0.05%
Michael J. McDevitt.................	13,900	0.1%
Executive Officers and Directors as a group (8 persons)	1,666,005	15.1%

*The address is c/o Medifast, Inc., 11445 Cronhill Drive, Owings Mills, Maryland 21117

(1) Mr. MacDonald beneficially owns 1,090,373 shares of common stock and 90,000 shares of voting Series "C" Preferred Convertible Stock. Mrs. Shirley D. MacDonald and Ms. Margaret E. MacDonald, wife and daughter of Mr. MacDonald, individually or jointly own 442,625 shares of stock.

PART IV

ITEM 13. EXHIBITS AND REPORTS ON FORM 8-K.

(a) Exhibits

3.1 Certificate of Incorporation of the Company and amendments thereto*

3.2 By-Laws of the Company*

10.1 1993 Stock Option Plan of the Company as amended*

10.3 Lease relating to the Company's Owings Mills, Maryland facility**

10.4 Employment agreement with Bradley T. MacDonald***

----

* Filed as an exhibit to and incorporated by reference to the Registration Statement on Form SB-2 of the Company, File No. 33-71284-NY.

** Filed as an exhibit to and incorporated by reference to the Registration Statement on Form S-4 of the Company, File No. 33-81524.

*** Filed as an exhibit to 10KSB, dated April 15, 1999 of the Company, file No. 000-23016.

21

(b) Reports on Form 8-K

March 23, 2004, to report the official 2004 financial guidance

July 2, 2004, to report the Company had decreased 2004 guidance

September 10, 2004 to report the Annual Meeting of Shareholders September 3, 2004

ITEM 14. ACCOUNTING FEES

In 2004, the Company incurred $70,000 in accounting fees as compared to $60,000 in 2003. These fees include work performed on quarterly audits and the preparation of the Company's 10-QSB's and 10-KSB.

22

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.

MEDIFAST, INC.
(Registrant)

BRADLEY T. MACDONALD

Bradley T. MacDonald
Chairman, CEO & CFO
Dated: May 27, 2005

Pursuant to the requirements of the Securities Exchange Act of 1934, the following persons on behalf of the Registrant and in the capacities and on the dates indicated have signed this Report below.

Name	Title	Date
BRADLEY T. MACDONALD Bradley T. MacDonald	Chairman of the Board, Director, Chief Executive Officer and Chief Financial Officer	May 27, 2005
SCOTT ZION Scott Zion	Director	May 27, 2005
/s/ MICHAEL C. MACDONALD Michael C. MacDonald	Director	May 27, 2005
/s/ MARY T. TRAVIS Mary T. Travis	Director	May 27, 2005
/s/ REV. DONALD F. REILLY, OSA Rev. Donald F. Reilly, OSA	Director	May 27, 2005

/s/ MICHAEL J. MCDEVITT --------------------------------- Michael J. McDevitt	Director	May 27, 2005
/s/ JOSEPH D. CALDERONE --------------------------------- Joseph D. Calderone	Director	May 27, 2005

Index to Exhibits

Exhibit Number	Description of Exhibit
31.1	Certification of Chief Executive Officer pursuant to Item 601(b)(31) of Regulation S-K, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification of Chief Financial Officer pursuant to Item 601(b)(31) of Regulation S-K, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Certification of Chief Executive Officer and Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

MEDIFAST, INC. AND ITS SUBSIDIARIES

CONTENTS

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

Board of Directors and Stockholders
Medifast, Inc.
Owings Mills, Maryland

We have audited the consolidated balance sheets of Medifast, Inc. and its subsidiaries as of December 31, 2004 and 2003, and the related consolidated statements of income, changes in stockholders' equity and comprehensive loss and cash flows for the years then ended. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with standards established by the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated 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 Medifast, Inc. and subsidiaries as of December 31, 2004 and 2003, and the consolidated results of their operations and their consolidated cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Bagell, Josephs & Company, LLC

Gibbsboro, New Jersey
March 4, 2005

MEDIFAST, INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS

	Decembe 200
ASSETS	
CURRENT ASSETS:	
Cash	$ 61
Accounts receivable-net of allowance for doubtful accounts of $87,000 and $55,000	1,06

Inventory	4,25
Investment securities	2,62
Deferred compensation	32
Prepaid expenses and other current assets	1,07
Current portion of deferred tax asset	1
TOTAL CURRENT ASSETS	9,97
Property, plant and equipment - net	8,69
Trademarks and intangibles - net	7,13
Deferred tax asset, net of current portion	9
Other assets	7
TOTAL ASSETS	$ 25,96
LIABILITIES AND STOCKHOLDERS' EQUITY	
CURRENT LIABILITIES:	
Accounts payable and accrued expenses	$ 94
Income taxes payable	67
Dividends payable	6
Line of credit	36
Current maturities of long-term debt	45
TOTAL CURRENT LIABILITIES	2,50
Long-term debt, net of current portion	4,25
TOTAL LIABILITIES	6,76
STOCKHOLDERS' EQUITY:	
Series B Convertible Preferred Stock; par value $1.00; 600,000 shares authorized; 300,614 and 403,734 shares issued and outstanding	30
Series C Convertible Preferred Stock; stated value $1.00; 1,015,000 shares authorized; 200,000 and 267,000 shares issued and outstanding	20
Common stock; par value $.001 per share; 15,000,000 shares authorized; 11,001,070 and 10,482,609 shares issued and outstanding	1
Additional paid-in capital	20,55
Accumulated comprehensive loss	(3
Accumulated deficit	(1,28
	19,74
Less: cost of 78,160 and 83,863 shares of common stock in treasury	(53
TOTAL STOCKHOLDERS' EQUITY	19,20
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	$ 25,96

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

MEDIFAST, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF INCOME

	YEARS ENDED DECEMBER 31, 2004	2003
Revenue	$ 27,340,000	$ 25,379,000
Cost of sales	(6,746,000)	(6,825,000)
GROSS PROFIT	20,594,000	18,554,000
Selling, general, and administration	(17,590,000)	(14,956,000)
INCOME FROM OPERATIONS	3,004,000	3,598,000
OTHER INCOME (EXPENSE):		
Interest expense	(245,000)	(150,000)
Interest income	154,000	110,000
Other expense	(7,000)	--
	(98,000)	(40,000)
NET INCOME BEFORE PROVISION FOR INCOME TAXES	2,906,000	3,558,000
Provision for income taxes	(1,159,000)	(1,148,000)
NET INCOME	1,747,000	2,410,000
Less: Preferred stock dividend requirement	(18,000)	(58,000)
NET INCOME ATTRIBUTABLE TO COMMON SHAREHOLDERS	$ 1,729,000	$ 2,352,000
Basic earnings per share	$ 0.16	$ 0.25
Diluted earnings per share	$ 0.14	$ 0.22
Weighted average shares outstanding -		
Basic	10,832,360	9,305,731
Diluted	12,413,424	10,952,367

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

MEDIFAST, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENT OF CHANGES IN STOCKHOLDERS' EQUITY AND COMPREHENSIVE LOSS

FOR THE YEARS ENDED 2004 AND 2003

	SERIES B PREFERRED STOCK		SERIES C PREFERRED STOCK			
	Number of Shares	Stated Value Amount	Number of Shares	Stated Value Amount	Number of Shares	Par Val $0.00 Amoun
Balance, December 31, 2002	521,290	$521,000	985,000	$985,000	7,204,693	$7,00
Preferred converted to Common	-117,556	-117,000	-718,000	-718,000	1,671,108	2,00
Options exercised to Common Stock					615,714	
Warrants Converted to Common Stock					288,724	
Common Stock issued to Directors, consultants and acquisitions					665,970	1,00
Common Stock issued for Series "C" dividend					36,400	
Dividend paid in stock						
Net Income						
Balance, December 31, 2003	403,734	404,000	267,000	267,000	10,482,609	10,00
Preferred converted to Common	-103,120	-103,000	-67,000	-67,000	340,240	
Options exercised to Common Stock					47,221	1,00
Warrants Converted to Common Stock					46,700	
Conversion of debt to equity					55,400	
Conversion of debt to equity out of Treasury					114,000	
Common stock issued to Consultants					15,500	
Shares issued out of Treasury						
Common Stock issued for Series "C" dividend					13,400	
Dividend paid in stock						
Net Income						
Balance, December 31, 2004	300,614	$301,000	200,000	$200,000	11,001,070	$11,00

	COMMON STOCK		
	Accumulated Comprehensive Loss	Treasury Total	Stock
Balance, December 31, 2002	$ -	$5,745,000	($167,000)
Preferred converted to Common			
Options exercised to Common Stock		590,000	-516,000
Warrants Converted to Common Stock		350,000	
Common Stock issued to Directors, consultants and acquisitions		8,717,000	
Common Stock issued for Series "C" dividend		18,000	
Dividend paid in stock		-45,000	
Net Income	-25,000	2,385,000	
Balance, December 31, 2003	-25,000	17,760,000	-683,000

Preferred converted to Common			
Options exercised to Common Stock		35,000	-31,000
Warrants Converted to Common Stock		125,000	-123,000
Conversion of debt to equity		28,000	
Conversion of debt to equity out of Treasury		114,000	166,000
Common stock issued to Consultants		93,000	135,000
Shares issued out of Treasury		-135,000	135,000
Common Stock issued for Series "C" dividend			
Dividend paid in stock		-11,000	
Net Income	-14,000	1,733,000	
Balance, December 31, 2004	($39,000)	$19,742,000	($536,000)

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

MEDIFAST, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOW

	Years Ended December 31, 2004	2003
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income	$ 1,747,000	$ 2,410,000
ADJUSTMENTS TO RECONCILE NET INCOME TO NET CASH PROVIDED BY OPERATING ACTIVITIES FROM OPERATIONS:		
Depreciation and amortization	1,310,000	677,000
Realized (gain) loss on investment securities	19,000	(1,000
Common stock issued for services	93,000	207,000
Net change in other comprehensive (loss)	(14,000)	--
Deferred income taxes	486,000	1,138,000
CHANGES IN ASSETS AND LIABILITIES:		
(Increase) in accounts receivable	(422,000)	(357,000
(Increase) in inventory	(1,263,000)	(1,729,000
(Increase) in prepaid expenses and other current assets	(143,000)	(687,000
(Increase) in deferred compensation	(100,000)	(350,000
(Increase) decrease in other assets	(25,000)	44,000
(Decrease) increase in accounts payable and accrued expenses	(460,000)	525,000
Increase in income taxes payable	674,000	--
NET CASH PROVIDED BY OPERATING ACTIVITIES	1,902,000	1,877,000
CASH FLOW FROM INVESTING ACTIVITIES:		
Maturities (purchase) of certificates of deposit	(112,000)	418,000
Sale (purchase) of investment securities, net	1,450,000	(3,982,000
Purchase of building	(566,000)	(1,823,000
Purchase of property and equipment	(1,490,000)	(1,309,000
Purchase of intangible assets	(2,792,000)	(2,458,000
NET CASH (USED IN) INVESTING ACTIVITIES	(3,510,000)	(9,154,000

CASH FLOW FROM FINANCING ACTIVITIES:		
Issuance of common stock, options and warrants	7,000	6,722,000
(Decrease) increase in line of credit, net	314,000	(36,000
Proceeds from long-term debt	475,000	2,669,000
Principal repayments of long-term debt	(1,089,000)	(346,000
Dividends paid on preferred stock	(11,000)	(45,000
NET CASH PROVIDED BY (USED IN) FINANCING ACTIVITIES	(304,000)	8,964,000
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	(1,912,000)	1,687,000
Cash and cash equivalents - beginning of the year	2,524,000	837,000
Cash and cash equivalents - end of year	$ 612,000	$ 2,524,000
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:		
Interest paid	$ 245,000	$ 154,000
Income taxes	$ --	$ --
SUPPLEMENTAL DISCLOSURE OF NON CASH ACTIVITY:		
Conversion of preferred stock B and C to common stock	$ 170,000	$ 835,000
Common stock for services	$ 93,000	$ 207,000
Common stock for intangibles and fixed assets	$ --	$ 1,949,000
Conversion of debt to equity	$ 307,000	$ --
Preferred Stock Dividends	$ 7,000	$ 18,000

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

F-6

MEDIFAST, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2004 AND 2003

NOTE A - BUSINESS

Medifast, Inc. (the "Company", or "Medifast") is a Delaware corporation, incorporated in 1980. The Company's operations are primarily conducted through five of its wholly owned subsidiaries, Jason Pharmaceuticals, Inc. ("Jason"), Take Shape for Life, Inc. ("TSFL"), Jason Enterprises, Inc., Jason Properties, LLC and Seven Crondall, LLC. The Company is engaged in the production, distribution, and sale of weight management and disease management products and other consumable health and diet products. Medifast, Inc.'s product lines include weight and disease management, meal replacement and sports nutrition products manufactured in a modern, FDA approved facility in Owings

Mills, Maryland.

The Company is engaged in the manufacturing and distribution of Medifast(R) and Hi-Energy(R) branded and private label weight and disease management products. These products are sold through various channels of distribution, to include medical professionals, weight loss clinics, direct consumer marketing supported via the phone and the web, supported by licensed, qualified medical practitioners including qualified health advisors. The processing, formulation, packaging, labeling and advertising of the Company's products are subject to regulation by one or more federal agencies, including the Food and Drug Administration, the Federal Trade Commission, the Consumer Product Safety Commission, the United States Department of Agriculture, and the United States Environmental Protection Agency.

NOTE B - SIGNIFICANT ACCOUNTING POLICIES

Significant accounting policies followed in the preparation of the consolidated financial statements are as follows:

[1] PRINCIPLES OF CONSOLIDATION AND BASIS OF PRESENTATION:

The consolidated financial statements include the accounts of the Company and its wholly owned subsidiaries, Jason Pharmaceuticals, Inc., Take Shape For Life, Inc., Seven Crondall Associates, LLC, Jason Properties, LLC and Jason Enterprises, Inc. All inter-company accounts have been eliminated.

[2] CASH AND CASH EQUIVALENTS:

For the purposes of the consolidated statements of cash flow, the Company considers all highly liquid debt instruments purchased with maturity of three months or less to be cash equivalents. At December 31, 2004, the Company had invested in four $100,000 certificates of deposit, of which three are considered cash equivalents.

At December 31, 2003, the Company had invested in four $100,000 certificates of deposit, which are considered cash equivalents. The Company also invested $465,000 in miscellaneous investments through Merrill Lynch. These investments are considered cash equivalents due to terms of maturity.

[3] ACCOUNTS RECEIVABLE:

Accounts receivable are recorded net of reserves for sales returns and allowances, and net of provisions for doubtful accounts. Allowances for sales returns and discounts are based on an analysis of historical trends, and allowances for doubtful accounts are based primarily on an analysis of aging accounts receivable balances and on the creditworthiness of the customer as determined by credit checks and analysis, as well as the customer's payment history.

[4] INVENTORY:

Inventory is stated at the lower of cost or market, utilizing the first-in, first-out method. The cost of finished goods includes the cost of raw materials, packaging supplies, direct and indirect labor and other indirect manufacturing costs.

[5] ADVERTISING:

Advertising costs such as preparation, layout, design and production of advertising are deferred. They are expensed when the advertisement is first used, except for the costs of executory contracts, which are amortized as performance under the contract is received. Advertising costs deferred at December 31, 2004 and 2003, were $478,000 and $295,000 respectively. Advertising expense for the years ended December 31, 2004 and 2003 amounted to $1,055,000 and $2,233,000, respectively.

NOTE B - SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

[6] PROPERTY, PLANT AND EQUIPMENT:

Property, plant and equipment are stated at cost less accumulated depreciation and amortization. The Company computes depreciation and amortization using the straight-line method over the estimated useful lives of the assets acquired as follows:

Building and building improvements	39 years
Equipment and fixtures	3-15 years
Vehicles	5 years

The carrying amount of all long-lived assets is evaluated periodically to determine whether adjustment to the useful life or to the unamortized balance is warranted. Such evaluation is based principally on the expected utilization of the long-lived assets and the projected undiscounted cash flows of the operations in which the long-lived assets are used.

[7] INCOME TAXES:

The Company accounts for income taxes in accordance with Statements of Financial Accounting Standards No. 109, "Accounting for Income Taxes," which requires an asset and liability approach to financial accounting and reporting for income taxes. Deferred income taxes and liabilities are computed annually for differences between the financial statement and the tax basis of assets and liabilities that will result in taxable or deductible amounts in the future based on enacted tax laws and rates applicable to the periods in which the differences are expected to affect taxable income. Valuation allowances are established when necessary to reduce deferred tax assets to the amount expected to be realized.

[8] EARNINGS PER COMMON SHARE:

Basic earnings per share is calculated by dividing net profit attributable to common stockholders by the weighted average number of outstanding common shares during the year. Basic earnings per share exclude any dilutive effects of options, warrants and other stock-based compensation, which are included in diluted earnings per share.

[9] REVENUE:

Revenue is recognized for product sales upon shipment and passing of risk to the customer and when estimates of discounts, rebates, promotional adjustments, price adjustments, returns, and other potential adjustments are reasonably determinable, collection is reasonably assured and the Company has no further performance obligations. These estimates are presented in the financial statements as reductions to net revenues and accounts receivable. Estimated sales returns, allowances and discounts are provided for.

NOTE B - SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Outbound shipping charges to customers and outbound shipping-related costs are netted and included in "cost of sales."

Returns - Consistent with industry practice, the Company maintains a return policy that allows its customers to return product within a specified period (30 days). Because the period of payment generally approximates the period revenue was originally recognized, refunds are recorded as a reduction of revenue when paid. The Company's estimate for returns is based upon its historical experience with actual returns. While such experience has allowed for reasonable estimation in the past, history may not always be an accurate indicator of future returns. The Company continually monitors its estimates for returns and makes adjustments when it believes that actual product returns may differ from the established accruals.

[10] 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 disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting periods. Actual results could differ from those estimates.

[11] FAIR VALUE OF FINANCIAL INSTRUMENTS:

The carrying amounts reported in the consolidated balance sheets for cash, certificates of deposit, accounts receivable, accounts payable and accrued liabilities approximate fair value because of the immediate or short-term maturity of the financial instruments.

The Company believes that its indebtedness approximates fair value based on current yields for debt instruments with similar terms.

[12] CONCENTRATION OF CREDIT RISK:

Financial instruments that potentially subject the Company to credit risk consist of cash, certificates of deposit, investment securities and trade receivables. Cash, certificates of deposit and investment securities at December 31, 2004 and 2003, include amounts deposited with multiple financial institutions that exceed the federal insurance coverage by $3,525,000 and $3,862,000, respectively. The Company markets its products primarily to medical professionals, clinics, and Internet medical sales and has no substantial concentrations of credit risk in its trade receivables.

As of December 31, 2004 and 2003, the Company had two customers that individually represented over 10% of the accounts receivable and in the aggregate, approximately 49% and 26% of the accounts receivable, respectively.

NOTE B - SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

[13] STOCK-BASED COMPENSATION:

The Company has adopted Statement of Financial Accounting Standards No. 123, "Accounting for Stock-Based Compensation" ("SFAS 123"). The provisions of SFAS 123 allow companies to either expense the estimated fair value of stock options or to continue to follow the intrinsic value method set forth in Accounting Principles Bulletin Opinion No. 25, "Accounting for Stock Issued to Employees" ("APB 25") but disclose the pro forma effects on net income had the fair value of the options been expensed. The Company has elected to continue to apply APB 25 in accounting for its employee stock option incentive plans.

MEDIFAST, INC. AND SUBSIDIARIES

STOCK OPTION PLAN

On October 9, 1993 and as amended in May 1995, the Company adopted a stock option plan ("Plan") authorizing the grant of incentive and nonincentive options for an aggregate of 500,000 shares of the Company's common stock to officers, employees, directors and consultants. Incentive options are to be granted at fair market value. Options are to be exercisable as determined by the stock option committee.

In November 1997, June 2002 and July 2003, the Company amended the Plan by increasing the number of shares of the Company's common stock subject to the Plan by an aggregate of 200,000 shares, 300,000 shares and 250,000 shares respectively.

The Company has elected to continue to account for stock option grants in accordance with APB 25 and related interpretations. Under APB 25, where the exercise price of the Company's employee stock options equals the market price of the underlying stock on the date of grant, no compensation is recognized.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2004 AND 2003

NOTE B - SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

[13] STOCK-BASED COMPENSATION: (CONTINUED)

If compensation expense for the Company's stock-based compensation plans had been determined consistent with SFAS 123, the Company's net income and net income per share including pro forma results would have been the amounts indicated below:

	Year Ended December 31 2004	2003
Net income:		
As reported	$1,747,000	$2,410,000
Total stock-based employee compensation expense determined under fair value based method for all awards, net of related tax effects	(108,000)	(403,000)
Pro forma	$1,639,000	$2,007,000
Net income per share:		
as reported:		
Basic	$ 0.06	$ 0.25
Diluted	$ 0.14	$ 0.22
Pro forma:		
Basic	$ 0.15	$ 0.21
Diluted	$ 0.13	$ 0.18

The pro forma effect on net income may not be representative of the pro forma effect on net income of future years due to, among other things: (i) the vesting period of the stock options and the (ii) fair value of additional stock options in future years.

For the purpose of the above table, the fair value of each option grant is estimated as of the date of grant using the Black-Scholes option-pricing model with the following assumptions:

	2004	2003
Dividend yield	0.0%	0.0%
Expected volatility	0.40	0.40
Risk-free interest rate	4.50%	3.00%-5.00%
Expected life in years	1-5	1-5

The weighted average fair value at date of grant for options granted during the years 2004 and 2003 were $8.60 and $5.32, respectively, using the above assumptions.

The following summarizes the stock option activity for the years ended December 31:

	2004 Shares	2004 Weighted Average Exercise Price	2003 Shares
Outstanding at beginning of year	439,455	$1.76	891,669
Options granted	30,000	8.60	163,500
Options reinstated	0	0.00	0
Options exercised	(47,221)	(1.19)	(615,714)
Options forfeited or expired	(32,837)	(7.01)	(0)
Outstanding at end of year	389,397	$1.51	439,455
Options exercisable at year end	350,336	$1.11	302,668
Options available for grant at end of year	860,603		810,545

MEDIFAST, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2004 AND 2003

NOTE B - SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

[13] STOCK-BASED COMPENSATION: (CONTINUED)

The following table summarizes information about stock options outstanding and exercisable at December 31, 2004:

	Options Outstanding			Options Exercisable	
Range of Exercise Prices	Number Outstanding	Weighted Average Contractual Life Remaining (in Years)	Weighted Average Exercise Price	Number Exercisable	Weighted Average Exercise Price
$0.25	150,000	1.0	$0.25	150,000	$0.25
$0.32	16,670	2.5	$0.32	16,670	$0.32

$0.50	100,000	1.6	$0.50	100,000	$0.50
$0.65	8,334	3.6	$0.65	8,334	$0.65
$0.80	16,666	3.3	$0.80	16,666	$0.80
$0.86	1,667	3.3	$0.86	1,667	$0.86
$1.23	6,668	3.5	$1.23	6,668	$1.23
$1.26	16,667	3.5	$1.26	16,667	$1.26
$1.60	8,334	3.6	$1.60	-	$1.60
$4.80	22,391	4.1	$4.80	15,999	$4.80
$8.26	2,000	4.2	$8.26	1,000	$8.26
$8.60	30,000	4.8	$8.60	9,999	$8.60
$11.15	10,000	4.3	$11.15	6,666	$11.15
	389,397	2.2	$1.51	350,336	$1.11

[14] SEGMENT INFORMATION

In 2004 and 2003, the Company's international joint venture arrangements for distribution of goods in the Asian market were responsible for the revenue recognition of approximately $488,000 and $2,000,000, respectively.

MEDIFAST, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2004 AND 2003

NOTE B - SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

[14] SEGMENT INFORMATION (CONTINUED)

In 2004 and 2003, the Company's retail distribution through the division of Consumer Choice Systems recognized revenue of $2,134,000 and $979,000 respectively.

[15] RECENT ACCOUNTING PRONOUNCEMENTS

In June 2001, the Financial Accounting Standards Board ("FASB") issued Statement No. 142 "Goodwill and Other Intangible Assets". This statement addresses financial accounting and reporting for acquired goodwill and other intangible assets and supersedes APB Opinion No. 17, "Intangible Assets". It addresses how intangible assets that are acquired individually or with a group of other assets (but not those acquired in a business combination) should be accounted for in financial statements upon their acquisition. This Statement also addresses how goodwill and other intangible assets should be accounted for after they have been initially recognized in the financial statements. The Company, in its acquisitions, recognized $893,850 of goodwill. The Company performs its annual impairment test for goodwill at year-end. As of December 31, 2004, the Company has determined that there is no impairment of its goodwill.

In addition, the Company has acquired other intangible assets, which include: customer lists, non-compete agreements, trademarks and patents. The non-compete agreements are being amortized over the legal life of the agreements ranging between 3 to 7 years. The customer lists are being amortized over a period ranging between 5 to 10 years based on management's best estimate of the expected benefits to be consumed or otherwise used up. Trademarks and patents are regularly reviewed to determine whether the facts and circumstances exist to indicate that the useful life is shorter than originally estimated or the carrying amount of the assets may not be recoverable. The Company assesses the recoverability of its trademarks and patents by comparing the projected discounted net cash flows associated with the related asset, over their remaining lives, in comparison to their respective carrying amounts. Impairment, if any, is based on the excess of the carrying amount over the fair value of those assets.

On July 20, 2000, the Emerging Issues Task Force issued EITF 00-14 "Accounting For Certain Sales Incentives" which establishes accounting and reporting requirements for sales incentives such as discounts, coupons, rebates and free products or services. Generally, reductions in or refunds of a selling price should be classified as a reduction in revenue. For SEC registrants, the implementation date is the beginning of the fourth quarter after the registrant's fiscal year end December 15, 1999. EITF 00-14 has been considered in the preparation of the consolidated financial statements.

In December 1999, the Securities and Exchange Commission issued Staff Accounting Bulletin ("SAB") No. 101, "Revenue Recognition in Financial Statements." SAB 101 provides guidance for revenue recognition under certain circumstances, and is effective during the first quarter of fiscal year 2001. SAB 101 has been considered in the preparation of the consolidated financial statements.

NOTE B - SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

[15] RECENT ACCOUNTING PRONOUNCEMENTS (CONTINUED)

In December 2002, the FASB issued Statement No. 148, "Accounting for Stock-Based Compensation-Transition and Disclosure", an amendment of FASB Statement No. 123"("SFAS 148"). SFAS 148 amends FASB Statement No. 123, "Accounting for Stock-Based Compensation," to provide alternative methods of transition for an entity that voluntarily changes to the fair value based method of accounting for stock-based employee compensation. It also amends the disclosure provisions of that Statement to require prominent disclosure about the effects on reported net income of an entity's accounting policy decisions with respect to stock-based employee compensation. Finally, this Statement amends Accounting Principles Board ("APB") Opinion No. 28, "Interim Financial Reporting", to require disclosure about those effects in interim financial information. SFAS 148 is effective for financial statements for fiscal years ending after December 15, 2002. The Company will continue to account for stock-based employee compensation using the intrinsic value method of APB Opinion No. 25, "Accounting for Stock Issued to Employees", but has adopted the enhanced disclosure requirements of SFAS 148.

In May 2003, the FASB issued SFAS Statement No. 150, "Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity". This Statement establishes standards for how an issuer classifies and measures certain financial instruments with characteristics of both liabilities and equity. It requires that an issuer classify a financial instrument that is within its scope as a liability (or an asset in some circumstances). This statement is effective for financial instruments entered into or modified after May 31, 2003, and otherwise is effective at the beginning of the first interim period beginning after June 15, 2003, except for mandatory redeemable financial instruments of nonpublic entities, if applicable.

It is to be implemented by reporting the cumulative effect of a change in an accounting principle for financial instruments created before the issuance date of the Statement and still existing at the beginning of the interim period of adoption. The adoption of this statement did not have a significant impact on the Company's results of operations or financial position.

In November 2002, the FASB issued Interpretation No. 45 ("FIN 45"), Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others. FIN 45 requires a company, at the time it issues a guarantee, to recognize an initial liability for the fair value of obligations assumed under the guarantees and elaborates on existing disclosure requirements related to guarantees and warranties. The recognition requirements are effective for guarantees issued or modified after December 31, 2002 for initial recognition and initial measurement provisions. The adoption of FIN 45 did not have a significant impact on the Company's results of operations or financial position.

In January 2003, the FASB issued FASB Interpretation No. 46 ("FIN 46"), Consolidation of Variable Interest Entities, an Interpretation of ARB No. 51. FIN 46 requires certain variable interest entities to be consolidated by the primary beneficiary of the entity if the equity investors in the entity do not have the characteristics of a controlling financial interest or do not have sufficient equity at risk for the entity to finance its activities without additional subordinated financial support from other parties. FIN 46 is effective for all new variable interest entities created or acquired after January 31, 2003.

NOTE B - SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

[15] RECENT ACCOUNTING PRONOUNCEMENTS (CONTINUED)

For variable interest entities created or acquired prior to February 1, 2003, the provisions of FIN 46 must be applied for the first interim or annual period beginning after June 15, 2003. The adoption of FIN 46 did not have a significant impact on the Company' results of operations or financial position.

[16] INVESTMENTS

In accordance with SFAS No. 115, "Accounting for Certain Investments in Debt and Equity Securities", securities are classified into three categories: held-to-maturity, available-for-sale and trading. The Company's investments consist of debt and equity securities classified as available-for-sale securities. Accordingly, they are carried at fair value in accordance with SFAS No. 115. Further, SFAS No. 115 the unrealized holding gains and losses for available-for-sales securities are excluded from earnings and reported, net of deferred income taxes, as a separate component of stockholders' equity, unless the loss is classified as other than a temporary decline in market value.

[17] RECLASSIFICATIONS

Certain amounts for the year ended December 31, 2003 have been reclassified to conform to the presentation of the December 31, 2004 amounts. The reclassifications have no effect on net income for the year ended December 31, 2003.

NOTE C - INVENTORY

Inventory consists of the following at December 31, 2004 and 2003:

	2004	2003
Raw materials	$ 1,085,000	$ 813,000
Packaging.......................	958,000	694,000
Finished goods	2,208,000	1,481,000
	$ 4,251,000	$ 2,988,000

MEDIFAST, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2004 AND 2003

NOTE D - PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment as of December 31, 2004 and 2003, consist of the following:

	2004	2003
Land	$ 650,000	$ 565,000
Building and building improvements	6,728,000	5,937,000
Equipment and fixtures	4,062,000	2,876,000
Vehicle	11,000	20,000
	11,451,000	9,398,000
Less accumulated depreciation and amortization	2,753,000	1,949,000
Property, plant and equipment - net	$ 8,698,000	$ 7,449,000

Substantially all of the Company's property, plant and equipment are pledged as collateral for various loans (see Note I).

Depreciation expense for the years ended December 31, 2004 and 2003 were $804,000 and $421,000, respectively.

NOTE E - TRADEMARKS

	AS OF DECEMBER 31, 2004		AS OF DECEMBER 31, 2003	
	GROSS CARRYING AMOUNT	ACCUMULATED AMORTIZATION	GROSS CARRYING AMOUNT	ACCUMULATED AMORTIZATION
Customer lists	$4,355,000	$ 394,000	$1,724,000	$ 150,000
Non-compete agreements	840,000	248,000	840,000	86,000
Trademarks and patents	1,703,000	12,000	1,541,000	14,000
Goodwill	894,000	--	894,000	
Total	$7,792,000	$ 654,000	$4,999,000	$ 250,000

AMORTIZATION EXPENSE FOR THE YEAR ENDED DECEMBER 31, 2004 AND 2003 WAS AS FOLLOWS:

	2004	2003
Customer lists	$ 244,000	127,000
Non-compete agreements	162,000	86,000
Trademarks and patents	--	14,000
Total Trademarks and Intangibles	$ 406,000	$ 227,000

Amortization expense is included in selling, general and administrative expenses.

MEDIFAST, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2004 AND 2003

NOTE F - ACCOUNTS PAYABLE AND ACCRUED EXPENSES

Accounts payable and accrued expenses as of December 31, 2004 and 2003 consist of the following:

	2004	2003
Trade payables	$ 343,000	$ 969,000
Accrued expenses and other	116,000	121,000
Accrued payroll and related taxes	215,000	96,000
Sales commissions payable	266,000	360,000
Deferred revenue	--	168,000
Total	$ 940,000	$1,714,000

NOTE G - OPERATING LEASES

The Company leases office space for its eleven corporately owned Hi-Energy Weight Control Clinics under lease terms ranging from one to five year leases commencing 2004. Monthly payments under the leases range in price from $1,120 to $2,695. The Company is required to pay property taxes, utilities, insurance and other costs relating to the leased facilities.

The following is a schedule by years of future minimum rental payments required under operating lease that have initial or remaining non-cancelable lease terms in excess of one year as of December 31, 2004:

For the Years Ending December 31,	
2005	$ 238,737
2006	208,605
2007	166,355
2008	121,871
2009	117,038
Total minimum payments required	$ 852,606

MEDIFAST, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2004 AND 2003

NOTE H - INCOME TAXES

At December 31, 2004 and 2003, the principal components of the net deferred tax assets are as follows:

	2004	2003
Net operating loss carry forwards	$ --	$ 290,000
Accounts receivable	19,000	32,000
Inventory overhead and write downs	--	274,000
Trademarks and intangibles	91,000	--
Total deferred tax assets	110,000	596,000
Current benefit	19,000	596,000
	$ 91,000	$ --

A reconciliation of the federal statutory rate to the income tax expense is as follows:

	Year Ended December 31, 2004	2003
Income tax based on federal statutory rate	$ 600,000	$ 973,000
State and local tax, net of federal benefit	90,000	175,000

Deferred income tax expense	469,000	--
Income tax expense	$ 1,159,000	$1,148,000

MEDIFAST, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2004 AND 2003

NOTE I - LONG-TERM DEBT AND LINE OF CREDIT

Long-term debt as of December 31, 2004 and 2003, consist of the following:

	2004	20
$2,850,000 fifteen year term loan secured by the building and land at a variable rate which was 5.14% at December 31, 2004	$ 2,391,000	$ 2,58
$1,760,000 ten-year reducing revolver line of credit rate at LIBOR plus 220 bps , which was 4.59% on December 31, 2004	1,623,000	1,74
$186,976 three-year term loan secured by 20,000 restricted common shares variable rate which was 8.25% at December 31, 2004	111,000	15
$200,000 five-year term loan secured by equipment fixed rate was 3% at December 31, 2004	130,000	17
$475,000 seven-year loan secured by the building and land at a variable rate at LIBOR plus 250 bps, which was 4.91% on December 31, 2004	459,000	
$220,000 two-year term loan secured by equipment at a floating rate which was 6% at December 31, 2003	--	7
$100,000 unsecured note payable at a fixed rate of 3%, discounted to an incremental borrowing rate of 12%	--	5
Note payable over 3 years secured by vehicle at a fixed rate of 12.25%	--	
$550,000 agreement three years secured by certain assets of the Company variable rate, which was prime floating at December 31, 2003.	--	55
	4,714,000	5,32
Less current portion	458,000	76
	$ 4,256,000	$ 4,56

Future principal payments on long-term debt for the next 5 years are as follows:

2005	$ 458,000
2006	475,000
2007	421,000
2008	376,000
2009	379,000
Thereafter	2,605,000

	$ 4,714,000

The Company has established a $5 Million revolving line of credit at the LIBOR rate plus 2% with Mercantile Safe Deposit and Trust Company secured by substantially all of the assets of Jason Pharmaceuticals, Inc. The outstanding balance on this line was $369,000 and $55,000 at December 31, 2004 and 2003, respectively. Effective January 17, 2004, $366,000 of the line of credit was converted to a note payable secured by all assets of Jason Pharmaceuticals excluding trade marks at a variable rate at libor plus 250 basis points which was 4.4% on December 31, 2004.

NOTE J - EMPLOYMENT AGREEMENTS

The CEO of Medifast, Inc., Bradley T. MacDonald, has a two-year employment agreement for an aggregate annual base salary of $225,000 with a bonus potential of 50% of base salary provided the Company makes its profit plan per the Board approved forecast. This contract has been extended to December 31, 2007. Due to the inequities of funding a retirement plan in the 401K, and in recognition of the performance responsible for the turnaround of the Company, the Board of Directors approved a Selective Executive Retirement Compensation Plan funded by the form of deferred compensation. The Deferred Compensation Plan will be funded up to $350,000 by a dollar for dollar match program, having Mr. MacDonald defer $175,000, followed by a Company match of $175,000. In June 2004 The Board of Directors authorized an additional $50,000 to be deferred by Mr. MacDonald followed by a Company match of $50,000. This brought the Selective Executive Retirement Compensation Plan total funded value to $450,000. Mr. MacDonald exercised 100,000 options at $.25 in January 2003 and 15,000 options at $.75 in March 2003. He has no options remaining available to exercise.

NOTE K - REDEEMABLE PREFERRED STOCK

In August 1996, the Company sold 432,500 shares of Series "A" nonvoting preferred stock that generated gross proceeds of $865,000, or $2.00 per share. Each share was entitled to a dividend of 8% ($.16) per share. The shares were convertible into the Company's common stock on the basis of one share of common stock for each share of convertible preferred stock. In 2001, 157,000 shares opted to convert to Series "C" Preferred Convertible Stock and 85,000 shares were redeemed under the partial settlement and conversion to Series "C" preferred convertible stock offered to Series "A" preferred stockholders as approved by the Board of Directors. In 2002 the remaining 75,000 shares were redeemed.

NOTE L - SERIES "B" CONVERTIBLE PREFERRED STOCK

In January 2000, the Company was authorized to issue 600,000 Series "B" Convertible Preferred Stock ("Preferred Stock B") par value $1.00 per share. Each share is entitled to a dividend of 10% of liquidation value $1.00 ($.10) per share and is to be converted on January 15, 2005 unless converted prior thereto. Each holder of Preferred Series "B" stock is entitled to four votes per share in all matters in which holders of the Company's common stock are entitled to vote. These shares were converted to common stock in January 2005. (See note Q).

Each share of Preferred Series "B" stock is convertible, at the option of the holder after one year from the issuance date into common stock of the Company. The initial conversion price will be 75% of the market value of the Company's common stock on the day prior to conversion with a maximum conversion price of $.50 per share subject to adjustment as defined. In March 2002, the Board amended the Series "B" convertible preferred stock terms and conditions as follows (1) a dividend of 10% paid in preferred stock, or (2) cash at the option of the holder. The Board also fixed the conversions of Series "B" preferred at $0.50 per share in common stock and eliminated the spiral conversion provision and reduced voting to 2 votes per share.

NOTE L - SERIES "B" CONVERTIBLE PREFERRED STOCK (CONTINUED)

Throughout the year of 2004, 103,120 shares of Series "B" Convertible Preferred Stock were converted into 206,240 shares of Common Stock. As of December 31, 2004 there were 300,614 shares of Series "B" Convertible Preferred Stock remaining.

NOTE M - SERIES "C" PREFERRED CONVERTIBLE STOCK

In the Fall of 2001, the Company was authorized to issue 1,015,000 shares of Series "C" Preferred Convertible Stock par value (.001), market value $1.00 per share. Each share is entitled to a dividend of 10% of liquidation value $1.00 ($.10) per share and is to be converted on December 31, 2006 unless converted prior thereto. Each Holder of Preferred Series "C" Stock is entitled to one (1) vote per share in all matters in which holders of the Company's Common Stock are entitled to vote. Each share of Preferred Series "C" Stock is convertible, at the option of the holder, after one year from the issuance date into Common Stock of the Company. The conversion price will be $.50 a share. In 2002, 11,500 warrants issued at $0.35 per share were distributed proportionately to Series "C' preferred holders.

Throughout the year of 2004, 67,000 shares of Series "C" Preferred Convertible Stock were converted into 134,000 shares of Common Stock. As of December 31, 2004 there were 200,000 shares of Series "C" Preferred Convertible Stock remaining.

NOTE N - WARRANTS

During 2003, the Company issued 200,000 warrants to James Paradis and Anthony Burrascono, both affiliated with Villanova University and 200,000 warrants to Mr. David Scheffler, an investment banker, for advisory and consulting services provided to the Company. The warrants vest in five equal installments of 40,000 warrants per year over a five-year period. These are five-year warrants to purchase common shares at an exercise price of $4.80 per share. These warrants may be cancelled, with a 90-day notice, if the consultants fail to perform to the satisfaction of the Company.

During 2003, the Company issued 50,000 warrants to Consumer Choices Systems, Inc. ("CCS") as part of the payment for the purchase of the assets of CCS. These warrants are three-year warrants to purchase common shares at an exercise price of $10.00 per share. Of this amount, 25,000 warrants were exercised in 2003.

During 2003, the Company issued 63,750 warrants and 18,750 warrants to Mainfield Enterprises, Inc. and Portside Growth & Opportunity Fund. These warrants are five-year warrants to purchase common shares at exercise prices of $16.78 per share, which was equal to one hundred fifteen percent (115%) of the five-day volume weighted average price, all pursuant to the terms of that certain Securities Purchase Agreement by and between the Company and Mainfield Enterprises, Inc. and Portside Growth & Opportunity Fund dated as of July 24, 2003.

NOTE N - WARRANTS (CONTINUED)

During 2004, there were 40,000 warrants exercised at $4.80 and 6,700 warrants exercised at $0.35.

The fair value of these warrants were estimated using the Black-Scholes pricing model with the following assumptions: interest rate 4.5%, dividend yield 0%, volatility 0.40 and expected life of five years.

The Company has the following warrants outstanding for the purchase of its common stock:

Exercise Price	Expiration Date	Year Ended December 31, 2004	2003
$0.35	August, 2004	--	40,100
$0.35	March, 2005	2,000	--
$0.625	September, 2004	--	2,500
$4.80	April, 2008	360,000	400,000
$10.00	June, 2006	25,000	25,000
$16.78	July, 2008	82,500	82,500
		469,500	550,100
	Weighted average exercise price	$7.16	$6.49

As of December 31, 2004, 229,500 of the warrants are exercisable.

NOTE O - COMMITMENTS, CONTINGENCIES AND OTHER MATTERS

The Company, like other manufacturers and distributors of products that are ingested, faces an inherent risk of exposure to product liability claims in the event that, among other things, the use of its products results in injury.

NOTE P - LITIGATION

On December 16, 2003 John Donavin, on behalf of the General Public, filed suit, against Jason Pharmaceuticals, Inc. in the Superior Court of the State of California, City and County of San Francisco. The suit alleges that Medifast bars contain Vitamin D3 or Vitamin D in violation of Federal laws and regulations, and asks for equitable relief and damages. The Company's general council believes that the Company's formulation used in its "meal replacement" bars for over 20 years has been and is in conformity with current and past FDA regulations. The Company believes that the plaintiff's claim lacks merit and may even be considered frivolous. The suit has been stayed upon appeal to the FDA to clarify its regulations.

NOTE P - LITIGATION (CONTINUED)

A former consultant continues to claim that he transferred his personal Medifast stock to a third party organization in 2000, in an attempt to keep these assets out of his bankrupt estate and therefore outside the jurisdiction of the Bankruptcy Court. The Company contests, and will vigorously defend, all such claims made by him. The Trustee in Bankruptcy for the former consultant's bankruptcy estate has determined that he had no authority to transfer these shares from his estate, and has concluded that the attempted transfer was therefore invalid. The Trustee has demanded that he produce the shares, and plans to file a petition with the Bankruptcy Court requesting that the Court order him to do so. These assets will be made a part of the bankrupt estate and will be used to pay creditors.

NOTE Q - SUBSEQUENT EVENTS

In January 2005, the remainder of the Series "B" Convertible Preferred Stock was converted to Common Stock in accordance with the terms and conditions of the original offering statement, dated January 19, 2000. The offering stated that the holders, at the time of conversion, are to receive a dividend at a rate of 10% per annum and that "interest" will be paid in Common Stock.