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HYDROMER INC
Form 10KSB
September 20, 2005

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON D. C. 20549

FORM 10-KSB

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

For the fiscal year ended June 30, 2005

Commission File Number 0-10683

HYDROMER, INC.

(Exact name of registrant as specified in its charter)

New Jersey

22-2303576

(State of incorporation)

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

35 Industrial Parkway, Branchburg, New Jersey

08876-3424

(Address of principal executive offices)

(Zip Code)

Registrant's telephone number, including area code:

(908) 722-5000

Securities registered pursuant to Section 12 (b) of the Act:

None

Securities registered pursuant to Section 12 (g) of the Act:

Common Stock Without Par Value

(Title of class)

Check whether the issuer (1) has filed all reports required to be filed by Section 13 or 15 (d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such report(s) and (2) has been subject to such filing requirements for the past 90 days. Yes (X) No ()

Check if there is no disclosure of delinquent filers in response to Item 405 of Regulation S-B is not contained in this form, and no disclosure will 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 (X)

The aggregate market value of the voting stock held by non-affiliates of the Registrant at September 1, 2005 was approximately \$5,086,336.

The number of shares of Registrant's Common Stock outstanding on September 1, 2005 was 4,623,942.

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Portions of the Audited Financials Statements for the year ended June 30, 2005 are incorporated by reference in Part II of this report. Portions of the Proxy Statement of Registrant dated September 15, 2005 are incorporated by reference in Part III of this report.

1

PART I

ITEM 1. BUSINESS

GENERAL

Hydromer, Inc (the "Company") is a polymer research and development company organized as a New Jersey Corporation in 1980 for the purposes of developing polymeric complexes for commercial use in the medical, commercial, cosmetics and veterinary sciences markets.

Until September 1982, approximately 99% of the outstanding common stock, without par value (the "Common Stock"), of the Company, was owned by Biosearch Medical Products Inc. ("BMPI"), which in turn was controlled by Manfred Dyck, who is the Company's current Chief Executive Officer, Director and the Chairman of the Board. On September 16, 1982, BMPI distributed its shareholdings in the Company pro rata to the holders of its common stock. In connection with this distribution, the Company granted to BMPI an exclusive, worldwide perpetual, royalty-free license for the use of Hydromer technology in connection with the development, manufacture and marketing of biomedical devices for enteral feeding applications. On February 4, 2000, the Company acquired all outstanding stock of BMPI for \$0.20 per share, and now manages BMPI as a subsidiary.

The Company owns several process and applications patents for Hydromer(R) coatings ("Hydromer"), which is a polymeric substance that becomes extremely lubricious (slippery) when wet, and a technique of grafting or applying this substance onto surfaces which may consist of a broad variety of materials, including other polymers like polyurethane, polyvinyl chloride, and silicone elastomers, ceramics and metals. The Company has also been issued patents for permanent anti-fog materials, hydrophilic polyurethane foams, hydrophilic polyurethane blends, hydrophilic polyvinylbutyral alloys, several biocompatible hydrogels and an anti-bacterial medical material. Currently, the Company has two patent applications pending. The Company continues to actively evaluate other new market opportunities for its polymer technology.

The Company also owns various trademarks, including AQUADAPT(R), a medical hydrogel, AQUAMERE(R), a water resistant film former product with cosmetic applications, AQUATRIX(R), a cosmetic hydrogel, Dermaseal(R), a dermal barrier film product for the prevention of contact dermatitis, Sea-Slide(R), a coating for watercraft hulls, and T-HEXX(R), a barrier teat dip product for the prevention of mastitis in dairy animals.

The Company's patents are typically broad based, having a multitude of different applications across various industries. Accordingly, the Company currently operates in the medical, commercial, cosmetics and veterinary sciences markets.

MEDICAL

From its inception in 1980 to mid-1984, the Company was primarily engaged in R&D activities related to Hydromer coatings used on medical devices. Since then and until the acquisition of BMPI, the Company's business in the medical field consisted of the sale of lubricious coatings and the licensing of its lubricious coating technologies. With the acquisition of BMPI in February 2000, the Company now offers a horizontally integrated breadth of services including medical

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device manufacturing, contract coating, equipment building and design, and as of more recently, R&D servicing and government contracts.

The Company continues to focus on its coatings technologies as the nucleus of its participation in the medical field. As of June 30, 2005, the Company has a patent pending on water-based lubricious coatings. The Company was granted a patent on a radio-opaque coating in 2004.

HYDROMER(R) LUBRICIOUS COATINGS

When treated with Hydromer polymers, a medical device becomes very slippery when wet, allowing for easy insertion into any orifice of the body, in penetration of the skin or for device-on-device (i.e. guidewire-catheter) use. Hydromer coatings are permanently bonded to the device unlike silicone lubricants, which must be applied after each use and are often left behind in the bloodstream and body cavities. Hydromer coatings can also be coated on complex surfaces and on the inside walls of devices, unlike the treatments by major competition. Hydromer has also been shown in numerous studies to reduce the risk of thrombogenesis or clot formation on devices. Drugs and other substances can be readily incorporated into Hydromer, both in a bound and unbound fashion, allowing for controlled release from the device for therapeutic purposes or the creation of permanent biocidal or biostatic surfaces. The Company believes that the polymer-water interface of Hydromer provides surface lubricity superior to the quality of other currently marketed silicone-based lubricants to treat medical devices.

OPTION AND LICENSE AGREEMENTS

A portion of the Company's revenues is derived from option and license agreements (see "Patents and Trademarks" section). Option agreements provide customers the right for a finite period of time (i) to use the Hydromer process to determine whether the customer's products lend themselves to treatment with the process and (ii) to test market such products. The option agreements have also given the customers the right to subsequently enter into a license agreement with the Company and to the market product(s) treated with Hydromer, which typically provides the Company an

2

initial flat fee, followed by periodic royalty payments based on sales.

The Company has previously reported license agreements in effect and expiring relating to applications of the Hydromer as follows: Annual Report on Form 10-K for the fiscal years ended June 30, 1983 through 1996 and Form 10-KSB for fiscal years ended 1997 through 2004.

As of June 30, 2005, the Company has license agreements with nine companies covering the application of Hydromer coatings to the following devices: enteral feeding products, guidewires, certain urological devices, infusion microcatheters, central venous catheters, guiding and umbilical catheters, razor cartridges (non-medical related), orthodontic accessories, angioplasty balloon catheters, embolization delivery devices, inter/intra-ocular lenses and biliary and pancreatic stents. The Company is actively seeking new licensing opportunities.

LICENSEE/APPLICATION

Applied Medical - certain urological and vascular devices
Becton-Dickinson - certain vascular devices with anti-microbial coatings
Corneal, Ltd. - inter-ocular lenses
Eveready - Schick / Warner / Wilkinson Sword Ltd. - razor cartridges

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Gallini - certain urological devices
MXM - intraocular lens inserter systems
Nemed - inter-ocular lenses
TP Orthodontics - certain orthodontic accessories
Tyco International / Kendall HealthCare Products - certain urological devices
and enteral feeding systems

HYDROGELS, DRUG DELIVERY, WOUND DRESSING

Applications of the Company's Hydrogels are being developed for wound care, implants, drug delivery, burn care, conductive hydrogel electrodes, ultrasonic couplants and cosmetic uses for several customers. The Company is also identifying strategic partners to offer hydrogel coating services to clients who does not have rolled goods coating capability and to license Hydrogel technology for cosmetic and medical use, including drug release.

The Company's hydrogel technology offers biocompatibility, flexibility, and ease of use and processing. It also allows for the stabilization of biomolecules, cell cultures, drugs and other active substances without potentially damaging external energy sources. It is absorbent, inherently self-adhesive but peels away cleanly and is naturally soothing. Other than our bio-adhesives and medical coatings, which are one part systems, to form the gel entails simply to mix the two parts together - no heat, no chemical cross linkers nor expensive high energy processing is required. Many competitive technologies are much more process intensive and require external energy to crosslink. The Company believes these products are synergistic to our existing hydrogel technologies, and offer further opportunities in electrodes and internal and topical actives delivery. The Company has a pilot coating machine to facilitate the commercialization of its hydrogel technologies. The Company is exploring other medical and dental as well as cosmetic applications for this technology.

Aquadapt(R) is the Company's hydrophilic polyurethane foam technology. The Company has 510K approvals from the FDA for medical use applications in the U.S. The Company also has a patent on its chitosan-PVP hydrogel technology as well as patents granted in 2000 and 2002 on polyaldehyde hydrogels.

OEM MEDICAL DEVICES

Through its Biosearch Medical Products subsidiary, ISO 13485 certified and FDA registered, the Company offers 510K/CE marked medical devices. The current product portfolio includes: bipolar coagulation probes; jejunal, enteral and biliary catheters and stents; feeding accessories; guidewires; biofeedback devices for fecal and urinary incontinence; and endoscopic accessories. The Company also contract manufactures products for several large multi-national marketers of medical devices on an OEM basis.

HYDROMER(R) COATING SERVICES

The acquisition of BMPI allowed for the Company to realize another venue of revenues: Coating Services. Utilizing the acquired medical device manufacturing know how and by applying its coatings technologies, the Company began offering Coating services, in which the Company coats third party devices with its own lubricious or third party coatings. The Company's knowledge in coatings technologies allows for it to coat various types of material, such as silicone, stainless steel, Pebax and polypropylene cost effectively, whereas some of the competition is unable to. A global client is using this service in the urology market.

The Company continues to expand its activity in Coating services and is actively seeking new opportunities to provide contract development, coating and manufacturing services to the medical, commercial and personal care industry, utilizing its Hydromer and Anti-Fog coating technology and expertise. The

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Company further continues to believe that these services will enable a broader range of customers to use our materials in market on accelerated timelines in a more cost effective manner.

R&D AND ENGINEERING SERVICES

The medical device market continues to undergo a shift toward consolidation by very large multi-national players with small, entrepreneurial start-up companies looking to exploit niche opportunities or unique device designs. The Company's experience and knowledge can

3

significantly speed development, assessment and market readiness for our clients, large and small through its research and development and engineering services.

For example, for medical devices such as coronary stents and brain catheters, the Company can develop the coatings, including drug eluting coatings, establish the manufacturing protocols, design and build the coating equipment, start up scale prototype production and eventually transfer the process assisting the customer in the transition.

The Company believes that offering prototyping, process development and small-medium scale coating/ manufacturing services is fundamental to the expansion of the Hydromer coatings business, and a strategic imperative. The Company will endeavor to become a "one stop" supplier of high performance coatings and services.

INDUSTRIAL/COMMERCIAL

Hydromer Anti-Fog/Condensation Control is an optical coating which prevents the accumulation of vision-obscuring condensation under high humidity conditions. The Company is selling this material in bulk to manufacturers of greenhouse panels, refrigerator freezer doors, industrial and medical safety and swim goggles, aircraft windows, automotive headlight assemblies and gauge and meter manufacturers in the U.S. and internationally, including China.

The Company also offers Sea-Slide(R), a Hydromer-based drag reducing coating that reduces friction between hull and water, and can be used over most anti-fouling paints. A U.S. patent covering this coating and other potential uses was issued in 1987. Independent testing has confirmed that this technology significantly improves fuel economy and the hull speed of watercraft. Sea-Slide is marketed through HammerHead Products, Inc., via an exclusive distribution agreement.

New food grade Anti-Fog coatings are in development for the ready-to-eat produce, meats and bakery products. The Hydromer Food Grade Anti-Fog is formulated with materials that are generally recognized as safe for food contact as confirmed by independent laboratory extraction testing. In early development are coatings for aluminum coils and cans.

COSMETICS

The Aquamere(R) series of the Company's cosmetic intermediaries are sold to major cosmetic companies worldwide for use in hair dyes, hair conditioners, mascaras, eye shadows, sunscreens and body lotions. They are currently in test for use in shampoos, hair styling aids, OTC dermal drug delivery and topical disinfectants. The Aquamere series of cosmetic polymer solutions, introduced in 1988, are both aqueous and hydro-alcoholic based systems. They are also offered with cationic and silicone grafted modifications. Formulations have also been

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developed internally utilizing this technology and are being offered for sale as turnkey products to smaller marketers of personal care products.

The Company's Dermaseal(R) line, a patented film-forming hydrogel technology, is currently being sold to major cosmetic companies as a base for foundations and other skin care products. It is also being tested for use in broader skin care, cosmetic and OTC drug delivery. Dermaseal is the registered trademark for barrier film compositions, patented in fiscal 2000 along with the method for preventing contact dermatitis. Clinical testing has demonstrated that these compositions protect the user from the effects of contact with poison ivy, oak or sumac plant allergens. Technical testing has also demonstrated protection from latex proteins, nickel and other contact allergens.

VETERINARY SCIENCES

In Fiscal Year 1999, the Company's polymer technology was used to launch the Company's entry into the Animal Health field to combat clinical and sub-clinical mastitis, a problem that costs U.S. Dairy farmers an estimated \$3-5 billion per year. Marketed under the T-HEXX(R) brand, initially through U.S. licensees, the T-HEXX Barrier Dips and Sprays offer dairy farmers exceptional value and unsurpassed protection as the first no-drip and water resistant barrier products on the market preventing environmental water containing mastitis-causing organisms, including mycoplasma, from reaching the teat surface. The Company has received three patents for its unique barrier teat dip compositions with an application on a fourth patent pending.

The annual U.S. market for barrier teat dips is estimated to be \$100-130 million at the farm level. The T-HEXX Barrier products contain protocol-proven active ingredients that kill mastitis-causing bacteria within 30 seconds of contact while continuing to remain active up to 12 hours later. T-HEXX Barriers are superior performers in its niche market while priced comparably or less than barrier dip products manufactured by the leading sanitary chemical companies in the world. Our products are compatible with existing mechanical equipment and milking procedures and most importantly, are easily removed using traditional pre-milking methods. Based on field tests, our product has been demonstrated to stay on the cow teat better than the competition, protecting the cow during the complete 8-12 hour milking cycle.

In fiscal 2002, the Company launched a complementary product, T-HEXX(R) Dry Teat Protection Sealant, to protect cows during the non-lactation ("dry cow") period. T-HEXX Dry is used as a non-irritating low-cost sealant

4

during the dry-off and the critical pre-calving period where it is estimated that over 50% of new mastitis cases are believed to start. T-HEXX Dry is the first dry cow dip product with an antimicrobial that remains on the teat for 3-7 days. Clinical studies show that T-HEXX Dry is impervious to National Mastitis Council (NMC) recognized mastitis-causing organisms for seven days, yet is comparably priced to existing dry cow teat sealants that does not offer such protection. Our product is suggested to be used on cows just prior to their release to the dry cow pen, in conjunction with existing antibiotic therapy or internal teat sealants. In fiscal 2004, two customers launched our Dry product under their private-label name, reflecting the strength of our product.

Patent pending and under development is a T-HEXX teat plug, which when launched, would allow the Company to provide complete protection against mastitis for the entire bovine working cycle.

The Company has invested significantly in clinical research, patents, promotion, vendor partnerships and advertising via print media, trade shows and the

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Internet to support this business and continues to do so. In fiscal 2004, the Company initiated a claim against a former licensee and other parties citing infringement on the Company's patented technology in this area. To date through June 30, 2005, the Company spent approximately \$253,000 (\$174,000 in fiscal 2005) in direct legal costs, which has been expensed in the related year's results. A mediation hearing held in September 2005 provided no results. Therefore the Company is pursuing the next course of action to protect its interests in its intellectual property.

PRODUCTS

Coating solutions for use on medical devices, cosmetic intermediaries, hydrogels and teat barrier dips/sprays are manufactured and sold by the Company to its licensees and others. The Company is selling bulk quantities of anti-fog solution to manufacturers of greenhouse panels, refrigerator freezer doors, swim goggles, industrial safety equipment, aircraft windows and meter covers, both in the U.S. and foreign countries. The Company also sells OEM medical devices through its Biosearch Medical Products subsidiary.

The Company has no long-term contracts with any of its suppliers and believes that there are adequate alternative sources of supply available for all raw materials that it currently uses.

DEPENDENCE UPON CUSTOMERS

The Company derives its revenues from two primary business segments: (1) polymer research and the products derived there from, and (2) the sales of medical products. During the fiscal years ended June 30, 2005 and June 30, 2004, the Company recognized revenues from two major customers: Johnson & Johnson's Cordis Division and Wilson Cook Medical, Inc.

Product sales and/or royalty payments from these customers accounted for 29% and 39% of the Company's total revenues for the years ended June 30, 2005 and June 30, 2004, respectively.

POTENTIAL APPLICATIONS

The Company continues to explore other applications of the complexing capabilities of polymeric substances, such as anti-microbial agents. The Company currently is working on further applications of its patented technologies to existing products of other companies, including cosmetics, wound dressings, personal care and a wide variety of medical devices, including vascular stents. Some of these products and applications are in the preliminary development stage and are subject to substantial further development before their feasibility can be verified.

On the basis of its market analyses, as well as laboratory and in-vitro testing of certain applications of Hydromer, the Company believes that Hydromer's potential product applications, classified with reference to salient Hydromer characteristics, are as follows:

1. LOW COEFFICIENT OF FRICTION. Hydromer is a hydrophilic coating which when contacted by water becomes extremely lubricious. The Company believes that this unique feature would prove beneficial to any medical device that is inserted into the body. Medical products that would so benefit include:

urinary products - urethral catheters, stents and urinary drainage systems;
rectal products - enemas, rectal tubes, examination gloves and proctoscopy devices (disposable);
nasal/oral products - suction catheters, oxygen catheters and endotracheal tubes;
cardiovascular and related products - grafts, cardiac assist catheters heart-lung tubing, stents.

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2. ABILITY TO BE COMPLEXED WITH OTHER FUNCTIONAL CHEMICALS. The Hydromer hydrophilic polymer coating can be complexed with other chemicals. For example, Hydromer coating complexed with iodine forms an effective anti-microbial barrier. The Company believes that this unique feature would lend itself to application on a wide variety of currently marketed medical products, including vascular stents, Foley catheters, wound drains, wart and corn dressings, burn dressings, intravenous catheters, surgical dressings and adhesive bandages. One of the Company's recent patents in the coating area, issued in April 2000, involves the covalent bonding of infection resistant materials into the coating, providing a non-leaching, anti-infective surface. The Company was also granted a patent in July 2003 for covalently bonded radio-opaque polymeric compositions to improve the radio-opacity of materials without needing high solid loading, metal plating or ion implantation for applications like stents and vascular catheters.

5

3. CROSS-LINK DENSITY CAN BE CONTROLLED. The Hydromer hydrophilic polymer coating, through controlled cross-linking, has been further developed into a special anti-fog coating. Such a coating is (a) resistant to fogging under a wide range of temperature/humidity conditions; (b) transparent and has heat/light stability; (c) long lasting, i.e., will not chip or peel and offers more scratch resistance than do most commercial plastics; (d) inert to most commercial glass cleaners; (e) less prone to static dirt pickup; and (f) applicable by dip, spray or roll coating. A U.S. Patent for this material was first issued to the Company in August 1984 (patent expired). This anti-fog product has use on greenhouse panels, refrigerator freezer doors, sports goggles, windows, mirrors and other products, either by direct application or by coating of an adhesive backed film. Food grade versions are available for packaging of fresh ready-to-eat produce, meats and deli-foods.

RESEARCH AND DEVELOPMENT

The Company's research and development activities presently are, and during the next year are expected to be devoted primarily to the development and enhancement of the products described above and to the design and development of new products, either for its own account, jointly with another company or strictly as a sub-contractor. The Company sponsors all of such activities from its own internal funding or through charges to the contracting company. The major portion of R&D expenses was applied toward salaries and other expenses of personnel employed on a regular basis in such work. See the "Employees" section.

COMPETITION

The Company considers the most significant competitive factors in its market for its patented coatings to be product capability and performance (including reliability and ease of use), in addition to price and terms of purchase.

The Company currently owns nineteen process and applications patents for Hydromer coatings (see "Patents and Trademarks"). Although the medical products market is highly competitive, the Company does not believe that there is any other product available which performs functions significantly better than those which are performed by the Company in terms of lubricity, complexing capabilities, durability and cost.

While management believes the Company has a strong position in the market for medical device coatings in which it competes, and that its hydrophilic foam, anti-fog coatings and hydrogel products are technologically superior to other products in the market, there can be no assurance that alternatives, with similar properties and applications, could not be developed by other companies. The Company is aware that there are other similar technologies available and/or being developed by others. The industry in which the Company competes is characterized by rapid technological advances and includes competitors that

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possess significantly greater financial resources and research and manufacturing capabilities, larger marketing and sales staffs and longer established relationships with customers than the Company does, at present or will for the foreseeable future.

MARKETING

The Company markets its products and services through five principal means:

1. **COMMERCIALIZATION OF ITS EXISTING TECHNOLOGIES:** The Company intends to expand its efforts to market its current technology to the medical, industrial, personal care and veterinary sciences markets. The Company has expanded its capabilities to prototype and manufacture for customers to demonstrate the value of Hydromer technology. The Company will also seek opportunities to apply its technology in new applications where the technology will offer a benefit. Further, the Company will seek customers for technologies that have been developed but are not currently generating revenue, capitalize on the technology that has been created through its R&D efforts and to expand the application of current technologies.

2. **SALE OF DEVELOPMENT SERVICES:** The Company intends to continue moving its effort away from straight technology licensing and toward contract product development, contract manufacturing and coating services (see "5. Coating Services"). The Company has significant expertise in polymer development and applications. By exhibiting at an increased number of trade shows in the medical device and cosmetic fields, the Company expects to generate interest in its technology and products, with a view toward acting as an outside product development arm and development supplier for companies in these fields.

3. **JOINT DEVELOPMENT:** The Company will continue to seek joint development programs, co-marketing programs and other business arrangements with potential partners.

4. **LICENSING:** The Company will continue its endeavors to license its technology to current market leaders in the medical device, pharmaceutical and other fields, whereby the Company will grant exclusive or non-exclusive rights for the Hydromer coating treatment of existing or new products, and the development of specific products utilizing its foam and hydrogel technology under its patents. In return, the Company generally would earn royalties based on sales of such treated or new products. Such licenses will usually be very narrow. The activities leading to the consummation of a license agreement normally are lengthy and require establishing a scientific dialogue with potential customers, treating samples supplied by that customer with Hydromer coatings, determining if the treatment is feasible and cost effective, testing the coated products in a laboratory and then negotiating a mutually acceptable option agreement. An

6

option fee may be paid by the customer which would give the customer exclusive rights to use the Hydromer treatment on the specified product for a specified period. During such period, the optionee can test market the coated product and/or determine its ability to treat the product in its own manufacturing process. If the customer determines that the subject product should be treated with Hydromer coating on a commercial basis, it may either perform the Hydromer coating treatment itself under a license agreement with the Company, through the Company's Contract Coating unit or it may have a third party perform the Hydromer coating treatment.

5. **COATING SERVICES:** The Company will serve the customer who needs products coated with lubricious or anti-fog coatings in production runs that are economically feasible without substantial investments in fixturing and

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automation. Typically this would be prototypes or runs of low volume, high value products. Higher volume products could be accommodated if they were physically small and did not require extensive fixturing or because for technical reasons they could not be automated and were of high enough value to warrant the added cost. The Company will pursue large volume projects if they fall within a technical area where the Company has particular expertise.

Business segments which are of particular interest include medical devices (catheters and guidewires) and transparencies (lenses, face shields). Contacts will be pursued in conjunction with marketing of Hydromer coatings, at trade shows, in mass mailings and advertisement in appropriate trade publications. The Company is continually upgrading its advertising copy and promotional literature as needed to graphically highlight the properties and advantages of its technologies.

The Company is focusing on expanding its global sales in markets where it has an established presence, and is increasing advertising and promotional activities via traditional means, including an expanded tradeshow presence in the U.S. and Europe, and the Internet to establish awareness of its technologies and capabilities in the medical, commercial, personal care and veterinary sciences community.

PATENTS AND TRADEMARKS

Management believes that the protection afforded by the Hydromer patents will be a significant factor in the Company's ability to market its products.

Anticipating patent expiration, the Company has focused on licensing and developing products based upon its newer technologies. The Company has also been issued United States and foreign patents for a permanent anti-fog. A U.S. patent was issued in October 1985 for a hydrophilic polyurethane foam that is expected to have numerous medical applications. Foreign patents covering this material were issued in July 1990. A U.S. patent for hydrophilic polymer blends, which covers the Company's coating for boats and the cosmetic formulations, was issued in February 1987. U.S. and foreign patents have also been issued for an anti-bacterial medical material that can be incorporated in foam or as a coating. The Company was issued a U.S. patent for non-leaching biostatic coatings and three United States patents for its new composition, barrier film, and method for preventing contact dermatitis developed by the Company's research and development staff. The Company has two patents for Chitosan gels, which expires in 2014. These patents are part of the new gel technology with applications in medical, industrial, cosmetic and personal care markets. The Company was issued three U.S. Patents for barrier teat dip compositions. One new patent was awarded to the Company during the fiscal year ended June 30, 2004.

As of June 30, 2005, the Company has 19 U.S. patents, two U.S. applications and various foreign counterparts. One U.S. patent, which contributed approximately \$2,000,000 in royalties annually, expired on May 6, 2005 and a second U.S. patent which contributes approximately \$65,000 in royalties annually, will expire in the fiscal year ending June 30, 2006. It is the Company's intention to replace any discontinuances of income stream with other sources, including new product revenues, new service revenues and other license revenues, including that from our patent pending water-based lubricious coatings. On September 1, 2005, the Company executed a three-year, 90-day termination notice, \$3,900,000 supply agreement (excludes the value of coatings to be sold) with a global pharmaceutical company, supplanting a majority of the royalties lost with the one U.S. patent expiration in May 2005.

The Company owns the registered trademarks "Aquadapt", "Aquamere", "Aquatrix", "Dermaseal", "Hydromer", "Sea-Slide" and "T-HEXX" in the United States and other countries.

EMPLOYEES

As of June 30, 2005, the Company and its subsidiary had eighty-six active

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full-time employees. The Chief Executive Officer is Manfred F. Dyck, who is also Chairman of the Board. The Company does not have a collective bargaining agreement with any of its employees and considers its relationship with its employees to be very good.

GOVERNMENT REGULATIONS

The uses of the Company's medical, agricultural and cosmetic products come under the jurisdiction of the FDA, as well as other federal, state and local agencies, and similar agencies in other countries.

In connection with the Company's license agreements, it is generally the obligation of the licensee to conform to any required FDA pre-market notification or other regulations. To the Company's knowledge, all such licensees who are marketing FDA regulated licensed

7

products are in such compliance. The Company may in the future desire to market additional applications of Hydromer to existing products, or products introduced by it, which may be subject to such FDA approval procedures as proof of safety and effectiveness of the applications or products, or adherence to prescribed design standards. There can be no assurance that such approvals would be forthcoming or of compliance with such standards. Any such failure to obtain approvals or non-compliance might have a significant adverse effect on the Company. However, the Company intends to make every effort to obtain all necessary approvals and to comply with such standards, and in the case of its licensed applications, to require the licensees to obtain such approvals.

The Company manufactures medical products through its Biosearch Medical Products subsidiary ("Biosearch"), whose activities come under the jurisdiction of the FDA. It is the policy of the Company to use the FDA regulations as guidelines during manufacturing of Hydromer coatings.

The Company is also subject to federal and state regulations dealing with occupational health and safety and environmental protection. It is the policy of the Company to comply with these regulations and be responsive to its obligations to its employees and the public.

The Company's electronically filed reports are available at WWW.SEC.GOV.

EXECUTIVE OFFICERS

The executive officers of the Company are as follows:

Name	Position with Company	Age as of Aug 31, 2005
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Manfred F. Dyck - Chairman of the Board, Chief Executive Officer and President		70
Martin C. Dyck - Executive Vice-President, Operations and President Biosearch Medical Products subsidiary		43
Rainer Gruening - Vice-President, Research & Development		62
John Konar - Vice-President, Quality Assurance and Director of Human Resources		56

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Robert Y. Lee - Vice-President, Finance,
Chief Financial Officer and Treasurer 39

Robert J. Moravsik - Senior Vice-President,
General Counsel and Secretary 62

Manfred F. Dyck has been Chairman of the Board of the Company since June 1983 and a Director of the Company since its inception. Mr. Dyck served as Chief Executive Officer of the Company from its inception until October 1986, and as of August 1989, reassumed the duties of Chief Executive Officer. Mr. Dyck was President of Biosearch Medical Products Inc. from 1975 until 1998 and a Director of Biosearch Medical Products Inc. from 1975 until 2000.

Martin C. Dyck has been Executive Vice-President, Operations since June of 2001. He was previously Vice-President of Operations since February 2000 when the Company purchased Biosearch Medical Products. Mr. Dyck has been President of Biosearch since 1998, a position which he still maintains. Mr. Dyck has been employed by Biosearch since 1986 and has served in various capacities including Director of New Product Development, where he developed several new medical devices and authored six FDA 510(k) pre-market submissions. After becoming President of Biosearch in 1998, Mr. Dyck changed the focus of Biosearch to become a contract medical coatings service provider using proprietary technology unique to Biosearch.

Rainer Gruening joined the Company as Vice-President of Research and Development in June 2001. With a PhD in Chemistry from the University of Marburg in Germany, his background includes service with Bayer AG/Deutsche Solvay Werke, Troy, G+G International and AM Cosmetics in areas including international regulatory affairs, coatings technology and anti-microbials. Mr. Gruening authored and/or co-authored 16 patents and 35 publications on synthesis and formulation of anti-microbials for paint and coatings, cosmetics, personal care products, adhesives, marine anti-fouling and metal working fluids and developed dossiers, safety assessments and GMP documentation. Additionally, he implemented FDA/CTFA, European and Japanese compliance requirements for raw materials and formulation restrictions.

John Konar has been the Vice-President of Quality Assurance since February 2004 and Director of Human Resources since February 2000. Mr. Konar joined Biosearch in 1986 and served as the Director of Human Resources with Biosearch from 1996 until its acquisition by the Company in 2000, when he then assumed responsibilities for both companies. He also served, with Biosearch, as the Director of Sales from 1996 until 2000, Director of Manufacturing from 2000 to 2001 and Director of QA from 1998 until 2004.

Robert Y. Lee joined the Company in the capacities of Vice-President of Finance, Chief Financial Officer and Treasurer in June 2001. He earned a MBA in Finance and International Business, and a Bachelors of Science in Accounting and Information Systems, both from New York University's Stern School of Business. His professional experience includes tenure with the New

8

York office of Coopers & Lybrand (currently PricewaterhouseCoopers) in their Emerging Business Group, the Bristol Myers Squibb Internal Auditing group, ASARCO's Southern Peru Copper Corporation and Citigroup.

Robert J. Moravsik has been Senior Vice-President, General Counsel and Secretary since February 2000. He holds a B.S. in Aerospace Engineering, an M.S. in Computer Science and a Doctorate in Law. He was Vice-President and General

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Counsel since April 1998. He also serves in the same capacity for Biosearch Medical Products, Inc. an affiliated company since 1987. Prior to that, he was Vice-President and General Counsel to Fisher Stevens, Inc., a subsidiary of the Bureau of National Affairs. He is an attorney admitted in the state of New Jersey and New York.

ITEM 2. PROPERTIES

In June 1998, the Company purchased the building and land at 35 Industrial Parkway, Branchburg, NJ from Biosearch Medical Products, then an affiliated party. The facility, currently its sole facility, is secured by mortgages through banks. See the financial statements included herein for the terms of the agreements.

In 2002, the Company completed its 10,400 square feet expansion at its primary location of 35 Industrial Parkway. This allowed the Company to consolidate certain manufacturing and quality assurance functions operations formerly located on leased space.

The expanded facility will be adequate for the Company's operations for the foreseeable future.

ITEM 3. LEGAL PROCEEDINGS

The Company is a plaintiff in a patent infringement action against a former licensee and a distributor of veterinary products. Counter claims have been filed against the Company alleging violation of anti-trust laws and inequitable conduct. The Company believes that these allegations are without merit.

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

Not applicable.

9

PART II

ITEM 5. MARKET FOR THE REGISTRANT'S COMMON EQUITY AND RELATED STOCKHOLDER MATTERS

Prior to January 9, 1986, the Company's Common Stock was traded in the over-the-counter market on the National Association of Securities Dealer's Automated Quotation System (NASDAQ) under the symbol "HYDI". Subsequent to January 9, 1986, reporting of trading was transferred to the National Daily Quotation Service (commonly known as the "Pink Sheets"). For the past nineteen years, trading in the Company's stock has been limited.

On February 13, 2002 the Company became a listed security on the Boston Stock Exchange ("BSX") under the trading symbol "HDO". Hydromer remains listed as "HYDI" on the OTC reporting services.

The Company's common stock traded at prices ranging between \$ 0.80 and \$3.05 in the fiscal year 2005 and between \$ 0.46 and \$2.00 in the fiscal year 2004. These prices may not include retail mark-ups or mark-downs or any commission to the broker dealer.

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The approximate number of holders of record of the Common Stock on September 1, 2005 was 235. There are approximately 700 individual shareholders of the common stock.

ITEM 6. MANAGEMENT DISCUSSION AND ANALYSIS

The below discussion analyzes major factors and trends regarding the results of operations and the financial condition of the Company as of June 30, 2005, and its results of operations for the prior fiscal period. It should be read in conjunction with the Financial Statements and Notes thereto.

REVENUES FOR THE YEAR ENDED JUNE 30, 2005 WERE \$8,486,004 AS COMPARED TO \$8,690,323 FOR THE SAME PERIOD LAST YEAR, A DECREASE OF \$204,319 (-2.4%).

Product sales and services revenues were \$6,185,622 for the 2005 fiscal year as compared to \$6,167,822 the prior fiscal year, a 0.3% increase or \$17,800.

License royalties and option payments were \$2,300,382 in fiscal 2005, down 8.8% from fiscal 2004's results of \$2,522,501.

MANAGEMENT COMMENT: Delayed customer orders negated the fiscal 2005 growth from our contract coating services and cosmetics line. During fiscal 2004, we had \$327,000 in private label sales against a delay in the current year's orders to fiscal 2006. The Company also had \$525,000 in engineering services in fiscal 2004, the project in which has been put on indefinite hold by the customer. While we look to recapture the delayed private label sales going forward, we supplanted the other drop in revenues from fiscal 2004 to fiscal 2005 through other projects and higher sales.

The Company's patent 4,642,267 (`267), the subject of four licenses with a total annual royalty income of approximately \$2.1 million, expired on May 6, 2005. Lost royalties arising from the expiration of this patent was approximately \$214,000 to fiscal 2005. On September 1, 2005, the Company entered into a supply agreement with one of the licensees on a three-year \$100,000 per month agreement, effective with the expiration of the related `267 patent. This agreement has a renewal option and is subject to cancellation with 90-days notice. The Company is also working with two other licensees on agreements post the `267 royalty licenses.

TOTAL EXPENSES FOR THE YEAR ENDED JUNE 30, 2005 WERE \$8,216,753, DOWN \$242,234 OR 2.9% FROM FISCAL YEAR 2004'S RESULTS OF \$8,458,987.

Cost of Goods Sold was \$3,228,875 for fiscal 2005 as compared to \$3,059,932 for fiscal 2004. Operating expenses were \$4,767,818 and \$4,720,864, for the years ended June 30, 2005 and 2004, respectively. The Provision for Income taxes was \$110,065 for the twelve months ended June 30, 2005 and \$317,519 for the twelve months ended June 30, 2004. Fiscal 2004 included a \$252,000 impairment of goodwill charge.

MANAGEMENT COMMENT: Although product and services revenues were flat between fiscal 2004 and fiscal 2005, the Cost of Sales was higher for fiscal 2005 primarily due to the higher costs of labor and fringe benefits. Operating expenses includes Employee costs and General expenses whose change between the fiscal years offset each other. In fiscal 2004, Employee costs were higher due to accrued bonuses arising from the strong year against the Board approved budget. The favorable year-on-year variance resulting from the lower employee costs to fiscal 2005 was offset by higher legal expenses relating to the patent infringement claim the Company initiated against a former licensee and other parties.

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Based on the evaluation of the Company's carrying value of goodwill, created from the acquisition of Biosearch in 2000, an impairment of goodwill of \$252,000 was warranted for the year ended June 30, 2004. There was no required charge for the year ended June 30, 2005. This charge in fiscal 2004 did not provide for a current tax benefit resulting in a higher tax provision. In addition, for fiscal 2005, we had a tax provision adjustment reducing our current year's tax expense.

10

NET INCOME FOR THE 2005 FISCAL YEAR WAS \$269,251 COMPARED TO \$231,336 FOR THE 2004 FISCAL YEAR, AN INCREASE OF \$37,915 (16.4%).

Net Income of \$269,251 or \$0.06 per share is reported for fiscal 2005 as compared with Net Income of \$231,336 or \$0.05 per share for fiscal 2004.

MANAGEMENT COMMENT: Although total revenues were lower by \$204,319 (2.4% off the previous fiscal year), total expenses were lower by \$242,234. Lower charges to fiscal 2005 (including the 2004 non-recurring goodwill impairment charge) more than offset the lower revenues. We continue to pursue additional revenue opportunities while seeking cost reduction initiatives.

LIQUIDITY AND CAPITAL RESOURCES

WORKING CAPITAL AS OF JUNE 30, 2005 WAS \$2,554,220, UP FROM \$1,670,604 THE PRIOR YEAR.

Working capital increased during the 2005 fiscal year due to the mortgage cash-out refinance in which an additional \$1,103,586 was made available to the Company for working capital needs, short-term investments and acquisitions.

MANAGEMENT COMMENT: We continue our re-investment back into the Company to support future growth of our business. The Company's Operating Assets and Liabilities (receivables, inventories, payables and accrued liabilities), net, were essentially unchanged from the previous year end, the primary change being the collection of receivables converted into higher inventory levels. Cash generated from operations (net income plus depreciation and amortization) plus the increase in our Deferred Revenues balance was used to fund the current period's Capital expenditures and patent estate in anticipation of future returns.

Management believes that the cash position along with short-term borrowings, will provide for sufficient funds to maintain its current level of operations.

ITEM 7. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

For information concerning this item, see pages F-1 through F-8 of the "Audited Financial Statements for the year ended June 30, 2005," which information is incorporated herein by reference.

ITEM 8. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

Not applicable.

PART III

ITEM 9. DIRECTORS AND EXECUTIVE OFFICERS OF THE REGISTRANT

For information concerning this item, see "Item 1. Business - Executive Officers" and pages 3 through 9 in the Proxy Statement filed with respect to the 2005 Annual Meeting of Shareholders (the "Proxy Statement"), which information is incorporated herein by reference.

ITEM 10. EXECUTIVE COMPENSATION

For information concerning this item, see page 7 of the Proxy Statement, which information is incorporated herein by reference.

ITEM 11. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT

For information concerning this item, see page 8 of the Proxy Statement, which information is incorporated herein by reference.

ITEM 12. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS

During the past fiscal year, there have been no related party transactions.

PART IV

ITEM 13. EXHIBITS, FINANCIAL STATEMENT SCHEDULES AND REPORTS ON FORM 8-K

(A) 1. FINANCIAL STATEMENTS:

The financial statements of the Company incorporated by reference in this Report are listed in the attached Index to the Financial Statements and Supplementary Data.

(A) 2. FINANCIAL STATEMENT SCHEDULES:

The financial statement schedules of the Company filed in this Report are listed in the attached Index to Financial Statements and Supplementary Data.

(A) 3. EXHIBITS (NOT INCLUDED)

The exhibits required to be filed as part of this Report are listed in the attached Index to Exhibits.

(B) CURRENT REPORTS ON FORM 8-K:

The Company filed a Form 8-K on July 6, 2005 announcing a loan agreement dated June 30, 2005.

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The Company and each person whose signature appears below hereby appoint Manfred F. Dyck and Robert Y. Lee as attorneys-in-fact with full power of substitution, severally, to execute in the name and on behalf of the registrant and each such person, individually and in each capacity stated below, one or more amendments to the annual report which amendments may make such changes in the report as the attorney-in-fact acting deems appropriate and to file any such amendment to the report with the Securities and Exchange Commission.

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.

HYDROMER, INC.

/s/ Manfred F. Dyck ----- Manfred F. Dyck	President, Principal Executive Officer, Chairman of the Board of Directors	September 12, 2005
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/s/ Robert Y. Lee ----- Robert Y. Lee	Chief Accounting Officer	September 9, 2005
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Pursuant to the requirements of the Securities and Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated:

/s/ Manfred F. Dyck ----- Manfred F. Dyck	President, Principal Executive Officer, Chairman of the Board of Directors	September 12, 2005
---	--	--------------------

/s/ Robert H. Bea ----- Robert H. Bea	Director	September 9, 2005
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/s/ Maxwell Borow ----- Maxwell Borow, MD	Director	September 13, 2004
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/s/ Ursula M. Dyck ----- Ursula M. Dyck	Director	September 13, 2005
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/s/ Dieter Heinemann ----- Dieter Heinemann	Director	September 12, 2005
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/s/ Klaus J.H. Meckeler ----- Klaus J.H. Meckeler, MD	Director	September 15, 2004
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/s/ Frederick L. Perl -----	Director	September 12, 2005
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Frederick L. Perl, MD

/s/ Michael F. Ryan

Director

September 12, 2005

Michael F. Ryan, PhD

13

HYDROMER, INC. & SUBSIDIARY
CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2005 AND 2004

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Stockholders of
Hydromer, Inc. and Subsidiary

We have audited the accompanying balance sheets of Hydromer, Inc. and Subsidiary as of June 30, 2005 and 2004 and the related statements of income, stockholders' equity and cash flows for each of the years in the two year period ended June 30, 2005. These financial statements are the responsibility of the company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Hydromer, Inc. and Subsidiary as of June 30, 2005 and 2004, and the results of its operations and its cash flows for each of the two in the two-year period ended June 30, 2005 in conformity with accounting principles generally accepted in the United States of America.

Rosenberg Rich Baker Berman & Company

Bridgewater, New Jersey
September 6, 2005

HYDROMER, INC. & SUBSIDIARY

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INDEX TO THE CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2005 AND 2004

	Page
Financial Statements	
Consolidated Balance Sheets.....	F-1
Consolidated Statements of Income.....	F-2
Consolidated Statements of Stockholders' Equity.....	F-2
Consolidated Statements of Cash Flows.....	F-3
Notes to the Consolidated Financial Statements.....	F-4 to F-8

HYDROMER, INC. & SUBSIDIARY CONSOLIDATED BALANCE SHEETS

2005

ASSETS

Current Assets:

Cash and cash equivalents.....	\$	1,376,656
Trade receivables less allowance for doubtful accounts of \$32,753 and \$10,727 as of June 30, 2005 and 2004, respectively.....		1,220,258
Inventory.....		1,094,927
Prepaid expenses.....		126,762
Deferred tax asset.....		91,989
Other.....		14,841

Total Current Assets.....		3,925,433
Property and equipment, net.....		3,276,258
Intangible Assets, net.....		780,140
Goodwill.....		238,172

Total Assets	\$	8,220,003
=====		

LIABILITIES AND STOCKHOLDERS' EQUITY

Current Liabilities:

Accounts payable.....	\$	466,993
Short-term borrowings.....		206,663
Accrued expenses		280,944
Bonus payable.....		77,267
Current portion of deferred revenue.. ..		161,317
Current portion of mortgage payable		178,029
Income tax payable.....		-

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Total Current Liabilities.....	1,371,213
Deferred tax liability.....	243,864
Long-term portion of deferred revenue.....	176,979
Long-term portion of mortgage payable	2,295,292

Total Liabilities	4,087,348

Contingencies	-
Stockholders' Equity	
Preferred stock - no par value, authorized 1,000,000 shares, no shares issued and outstanding	-
Common stock - no par value, authorized 15,000,000 shares; as of June 30, 2005, 4,634,859 shares issued and 4,623,942 shares outstanding; as of June 30, 2004, 4,608,904 shares issued and 4,597,987 shares outstanding.....	3,631,615
Contributed capital.....	577,750
Accumulated deficit.....	(70,570)
Treasury stock, 10,917 common shares at cost.....	(6,140)

Total Stockholders' Equity	4,132,655

Total Liabilities and Stockholders' Equity	\$ 8,220,003
=====	

SEE NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS.

F-1

HYDROMER, INC. & SUBSIDIARY
CONSOLIDATED STATEMENTS OF INCOME

	2005	Ye

REVENUES		
Sale of products.....	\$ 4,855,913	
Service revenues.....	1,329,709	
Royalties, options and licenses.....	2,300,382	

TOTAL REVENUES.....	8,486,004	

EXPENSES		
Cost of Sales.....	3,228,875	
Operating Expenses.....	4,767,818	
Impairment of Goodwill.....	-	
Other Expenses.....	109,995	
Provision for Income Taxes.....	110,065	

TOTAL EXPENSES.....	8,216,753	

NET INCOME	\$ 269,251	
=====		

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Earnings Per Common Share.....	\$	0.06
Earnings Per Common Share - Assuming Dilution.....	\$	0.06
Weighted Average Number of Common Shares Outstanding.....		4,614,500
Weighted Average Number of Common Shares Outstanding - Assuming Dilution.....		4,781,500

=====

SEE NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS.

HYDROMER, INC. & SUBSIDIARY
CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY

	Common Stock		Contributed	Accumulated	Treasu
	Shares	Amount	Capital	Deficit	Shares
Balance June 30, 2003	4,598,904	\$ 3,608,118	\$ 577,750	\$ (571,157)	10,917
Exercise of Stock Options	10,000	7,497			
Net Income				231,336	
Balance June 30, 2004	4,608,904	\$ 3,615,615	\$ 577,750	\$ (339,821)	10,917
Exercise of Stock Options	25,955	16,000			
Net Income				269,251	
BALANCE JUNE 30, 2005	4,634,859	\$ 3,631,615	\$ 577,750	\$ (70,570)	10,917

=====

SEE NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS.

F-2

HYDROMER, INC. & SUBSIDIARY
CONSOLIDATED STATEMENTS OF CASH FLOWS

CASH FLOWS FROM OPERATING ACTIVITIES:

Net Income.....	\$
Adjustments to reconcile net income to net cash provided by operating activities	
Depreciation and amortization.....	
Impairment of Goodwill.....	
Deferred income taxes.....	

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Changes in Assets and Liabilities	
Trade receivables.....	(
Inventory.....	(
Prepaid expenses.....	(
Other assets.....	(
Accounts payable and accrued liabilities.....	(
Deferred revenues.....	(
Income taxes payable.....	(

Net Cash Provided by Operating Activities.....	

CASH FLOWS FROM INVESTING ACTIVITIES:	
Cash purchases of property and equipment.....	(
Cash payments on Patents and Trademarks.....	(

Net Cash Used for Investing Activities.....	(

CASH FLOWS FROM FINANCING ACTIVITIES:	
Net borrowings/(payments) against Line of Credit.....	
Proceeds from long-term borrowings.....	1,
Repayment of long-term borrowings.....	(
Proceeds from the issuance of common stock.....	

Net Cash Provided by (Used for) Financing Activities.....	1,

NET INCREASE IN CASH AND CASH EQUIVALENTS:	
Cash and Cash Equivalents at Beginning of Period.....	1,

Cash and Cash Equivalents at End of Period.....	\$ 1,
=====	
Cash paid during the year for:	
Interest	\$
Income taxes	\$

SEE NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS.

F-3

HYDROMER, INC. & SUBSIDIARY
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

NATURE OF OPERATIONS

Hydromer, Inc. & Subsidiary (the "Company") is a polymer research and development company based in Branchburg, New Jersey. The Company develops polymer complexes for commercial markets in both the United States and abroad for the medical, cosmetics, veterinary sciences and industrial fields. The Company obtains patent rights on certain products from which royalty revenues are received. Its wholly owned subsidiary, Biosearch Medical Products, Inc., a U.S. based corporation, is an OEM manufacturer for various medical products companies as well as the manufacturer of its own line of endoscopic products sold to hospitals, domestically and internationally, through a network of dealers. The Company also offers R&D, engineering and contract coating services

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in its array of capabilities.

PRINCIPLES OF CONSOLIDATION

The consolidated financial statements include the accounts of Hydromer, Inc. and its wholly owned subsidiary. All significant intercompany balances and transactions have been eliminated.

CASH AND CASH EQUIVALENTS

Cash and cash equivalents consist of short-term investments with original maturities of three months or less.

SHORT-TERM INVESTMENTS

Short-term investments consist of investments other than cash and cash equivalents with original maturities of greater than three months and less than one year. As of June 30, 2005, there were no short-term investments.

INVENTORIES

Inventories are valued at the lower of cost, determined by the first-in, first-out method, or market and include appropriate amounts of labor and overhead.

DEPRECIATION

The cost of property and equipment, which includes a reasonable portion of labor costs for equipment built in-house, is depreciated on a straight-line method over the estimated useful lives of the assets: 5-10 years for machinery and equipment, 3-5 years for furniture and office equipment and 40 years for the building. When assets are retired or otherwise disposed of, the cost and related accumulated depreciation are removed from the accounts, and any resulting gain or loss is reflected in income for the period. Repairs and maintenance which do not extend the useful lives of the related assets are expensed as incurred.

PATENTS

Expenses associated with patents are prepaid and amortized over the expected life of the patent, typically 20 years. Prepaid expenses associated with patents which are not approved or abandoned are expensed in the period in which such patents are not approved or abandoned. Maintenance fees associated with existing patents are written off over 12 months. Amortization expense for the years ended June 30, 2005 and 2004 were \$69,665 and \$50,296, respectively. One new patent was approved during the year ended June 30, 2004.

GOODWILL

Goodwill represents the excess of the purchase price of Biosearch Medical Products, Inc. over the fair market value of their net assets at the date of acquisition and through June 30, 2002, was amortized on the straight line method over 40 years. The Company adopted Statement of Financial Accounting Standards ("SFAS") No. 142, GOODWILL AND OTHER INTANGIBLE ASSETS, on July 1, 2002 in which goodwill is no longer amortized but tested for impairment on at least an annual basis. The carrying value is reviewed if the facts and circumstances, such as significant declines in sales, earnings or cash flows or material adverse changes in the business climate, suggest that it may be impaired. If this review indicates that goodwill will not be recoverable, the impairment is determined by comparing the carrying value of goodwill to fair value. Fair value can be determined based on quoted market values, discounted cash flows or appraisals. The Company uses the present value of expected future cash inflows method.

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During the year ended June 30, 2004, the Company determined that the carrying amount of the goodwill exceeded its fair value by \$252,000. A goodwill impairment loss was recognized for that difference. For the year ended June 30, 2005, the Company determined that the fair value exceeded the carrying amount of the goodwill. Accordingly, there was no goodwill impairment charge required for the year ended June 30, 2005.

LONG-LIVED ASSETS

The Company assesses long-lived assets for impairment as required under SFAS No. 144, ACCOUNTING FOR THE IMPAIRMENT OR DISPOSAL OF LONG-LIVED ASSETS. The Company reviews for impairment whenever events or circumstances indicate that the carrying amount of these assets may not be recoverable. The Company assesses these assets for impairment based on estimated future cash flows from these assets.

REVENUE RECOGNITION

Revenues from product and services sales are recognized at the time of shipment or services rendered provided that collection of the resulting receivable is probable. Revenues from royalties are recognized upon the sale of certain products by licensees with whom the Company has licensing agreements. Deferred revenues are recorded when agreements call for payment ahead of when the amounts are earned.

SHIPPING AND HANDLING CHARGES

The Company includes costs of shipping and handling billed to customers in Revenues and the related expense of shipping and handling costs in Cost of Sales.

ADVERTISING

Advertising costs are expensed as incurred except for tangible assets, such as printed advertising materials, which are expensed as consumed. Advertising expense was \$47,267 and \$26,978 for the years ended June 30, 2005 and 2004, respectively.

RESEARCH AND DEVELOPMENT

Research and development costs are charged to operations when incurred and are included in operating expenses. The amounts charged to expense for the years ended June 30, 2005 and 2004 were approximately \$1,040,110 and \$670,154, respectively.

STOCK-BASED COMPENSATION

As permitted by SFAS No. 123, ACCOUNTING FOR STOCK-BASED COMPENSATION, the Company has elected to follow Accounting Principle Board Opinion No. 25, ACCOUNTING FOR STOCK ISSUED TO EMPLOYEES, ("APB 25") and related interpretations in accounting for its employee stock option plans. Under APB 25, no compensation expense is recognized at the time of option grant when the exercise price of the Company's employee stock options equals the fair market value of the underlying common stock on the date of grant.

INCOME TAXES

Income taxes are provided for the tax effects of transactions reported in the financial statements and consist of taxes currently due plus deferred taxes related primarily to differences between the bases of assets and liabilities for financial and income tax reporting. The deferred tax assets and

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liabilities represent the future tax return consequences of those differences, which will either be taxable or

F-4

HYDROMER, INC. & SUBSIDIARY NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

deductible when the assets and liabilities are recovered or settled. Deferred taxes also are recognized for operating losses that are available to offset future federal and state income taxes.

EARNINGS PER SHARE

Earnings per share, in accordance with the provisions of SFAS No. 128, Earnings Per Share, is computed by dividing net income by the weighted average number of common stock shares outstanding during the period.

USE OF ESTIMATES

The preparation of financial statements in conformity with generally accepted accounting principles 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 period. Actual results could differ from those estimates.

RECLASSIFICATION

Certain amounts previously reported have been reclassified to conform to the 2005 presentation.

2. NEW ACCOUNTING PRONOUNCEMENTS

In December 2004, the Financial Accounting Standards Board issued SFAS No. 123(R), SHARE-BASED PAYMENT, which establishes standards for transactions in which an entity exchanges its equity instruments for goods or services. This standard requires an issuer to measure the cost of employee services received in exchange for an award of equity instruments based on the grant-date fair value of the award. This eliminates the exception to account for such awards using the intrinsic method previously allowable under APB No. 25. In March 2005, the SEC released Staff Accounting Bulletin 107, SHARE-BASED PAYMENT, which expresses views of the SEC Staff about the application of SFAS No. 123(R). In April 2005 the SEC issued a rule that SFAS No. 123(R) will be effective for public entities that file as small business issuers--as of the beginning of the first interim or annual reporting period that begins after December 15, 2005. The adoption of SFAS No. 123(R) requires all equity compensation to be expensed during the related periods.

3. CONCENTRATION OF CREDIT AND BUSINESS RISK

The Company is exposed to additional credit and business risks due to its concentration of activity with certain parties. For example, at times throughout the year, the Company may maintain certain bank accounts in excess of FDIC insured limits.

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In addition, the Company provides credit in the normal course of business to customers. Ongoing credit evaluations of its customers are performed, and allowances for doubtful accounts are based on factors surrounding the credit risk of specific customers, historical trends and other information.

For the year ended June 30, 2005, the Company sold products and services and collected royalty income, totaling 29% of its total revenues, to two customers, Cordis Neurovascular Systems and Wilson Cook Medical, Inc. who individually accounted for 15% and 14%, respectively, of the consolidated revenues. Accounts receivable from these customers accounted for 22% of total accounts receivable at June 30, 2005.

During the fiscal year ended June 30, 2004 Cordis Neurovascular Systems and Wilson Cook Medical, Inc. individually accounted for 24% and 15%, respectively, of total revenues. Accounts receivable from these customers accounted for 53% of total accounts receivable at June 30, 2004.

The Company's patent 4,642,267 expired on May 6, 2005. This patent was the subject of four licenses with a total annual royalty income to the Company of approximately \$2.1 million. However, the Company was able to enter into a supply agreement with one of the licensees, valued at \$1.2 million annually, (see Footnote 16. SUBSEQUENT EVENTS) and is in discussions with two other licensees. Two other of the Company's patents (no. 4,769,013 and 4,875,287) will expire in June and November of 2006, respectively. Total annual royalty income from these patents, from four licenses, approximates \$0.1 million.

4. INVENTORY Inventory consists of:

	June 30,	
	2005	2004
Finished goods	\$ 336,078	\$ 169,779
Work in process	314,345	323,423
Raw materials	444,504	315,787
	\$ 1,094,927	\$ 808,989
	=====	=====

5. PROPERTY AND EQUIPMENT

Property and equipment consists of the following:

	June 30,	
	2005	2004
Land	\$ 472,410	\$ 472,410
Building	2,121,092	1,953,042
Machinery and equipment	3,556,839	3,189,482
Furniture and fixtures	733,595	708,725
	6,883,936	6,323,659
Less: Accumulated depreciation and amortization	(3,607,678)	(3,402,099)

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Property and Equipment, net	\$ 3,276,258	\$ 2,921,560
	=====	=====

Depreciation expense charged to operations was \$205,579 and \$194,908 for the years ended June 30, 2005 and 2004, respectively.

6. INTANGIBLE ASSETS

Intangible Assets are comprised of the following:

	June 30,	
	2005	2004
	-----	-----
Patents	\$ 975,940	\$ 800,334
Trademarks	72,412	70,010
Less: Accumulated amortization	(268,212)	(194,053)
	-----	-----
Intangible Assets, net	\$ 780,140	\$ 676,291
	=====	=====

Future amortization of the Intangible Assets, as of June 30, 2005, are as follows:

Year ending June 30,

2006	\$ 67,919
2007	66,376
2008	63,448
2009	62,108
2010	42,309
Thereafter	477,980

	\$ 780,140
	=====

F-5

HYDROMER, INC. & SUBSIDIARY
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

7. LONG-TERM DEBT AND CREDIT FACILITY

The Company's facility is financed by a ten-year mortgage note bearing interest at a 6.52% fixed rate. The note amortizes with monthly payments and is secured by the real estate and improvements and all rents from leases subsequently entered into.

On June 30, 2005, the Company closed on a long-term financing facility of \$1,990,000 in the form of a second mortgage on its property. This facility

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has a ten year term with a 6.38% fixed rate. \$886,414 was used to pay off a construction loan/continuing loan provided by New Millennium Bank with the remainder put in short-term investments or to be used for working capital and possible acquisitions. The facility was financed through Wachovia Bank, NA which also holds a \$555,000 first Mortgage on the Company's property.

In addition, the Company has a revolving line of credit agreement with a financial institution, which allows borrowings of up to \$750,000, secured by all trade receivables and inventories. The line bore interest, payable monthly at LIBOR plus 3.15% until June 2005 at which was then reduced to LIBOR plus 2.25%. As of June 30, 2005, the interest rate was 5.59%. This line had a maturity date of July 31, 2005 which was extended until November 30, 2005 during the year at the same terms. As of June 30, 2005 and 2004, \$206,663 and \$131,010 were outstanding on the line of credit respectively.

Long-term debt is comprised of the following:

	June 30,	
	2005	2004
Mortgage note	\$ 483,321	\$ 525,530
Second Mortgage Loan	1,990,000	929,700
Less: Current Maturities	(178,029)	(91,507)
Long-term Debt,		
Net of Current Maturities	\$ 2,295,292	\$ 1,363,723

Total maturities of long-term debt are as follows:

Year ending June 30,

2006	\$ 178,029
2007	202,204
2008	215,393
2009	230,182
2010	245,604
Thereafter	1,401,909
	\$ 2,473,321

8. FAIR VALUE OF FINANCIAL INSTRUMENTS

The carrying amount of cash and cash equivalents, short-term investments, accounts receivable, accounts payable and accrued expenses approximates fair value because of the short maturity of these instruments. The fair value of the Company's long-term debt approximates its carrying value as it is based on or about at the current rates offered to the Company for debt of the same remaining maturities with similar collateral requirements.

LIMITATIONS

Fair value estimates are made at a specific point in time, based on

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relevant market information about the financial instrument. These estimates are subjective in nature and involve uncertainties and matters of significant judgment and therefore cannot be determined with precision. Changes in assumptions could significantly affect the estimates.

F-6

HYDROMER, INC. & SUBSIDIARY NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

9. INCOME TAXES

The income tax provision is comprised of the following:

	Federal	State	Total
	-----	-----	-----

YEAR ENDED JUNE 30, 2005			
CURRENT	\$ 1,513	\$ 5,764	\$ 7,277
DEFERRED	90,843	11,945	102,788
	-----	-----	-----
	\$ 92,356	\$ 17,709	\$ 110,065
	=====	=====	=====
Year Ended June 30, 2004			
Current	\$ 77,606	\$ 21,699	\$ 99,305
Deferred	174,985	43,229	218,214
	-----	-----	-----
	\$ 252,591	\$ 64,928	\$ 317,519
	=====	=====	=====

The Company's deferred tax asset and liability as presented in the Company's financial statements are comprised of the following temporary differences:

	June 30,	
	2005	2004
	-----	-----

Deferred Tax Asset		
Net Operating Losses	\$ 201,628	\$ 207,382
Adjustment of Goodwill	100,800	100,800
Research & Development Credits	9,829	27,500
Valuation allowance	(220,268)	(193,884)
	-----	-----
Total Deferred Tax Assets	91,989	141,798
	=====	=====
Deferred Tax Liability		
Depreciation	(243,864)	(191,500)
	-----	-----
Total Deferred Tax Liability	\$ (243,864)	\$ (191,500)
	=====	=====

Deferred taxes are recognized for temporary differences between the bases of assets and liabilities for financial statement and income tax purposes. The differences relate primarily to depreciable assets (using accelerated depreciation methods for income tax purposes). The Company's adjustment to

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Goodwill in 2004 created a deferred tax asset, which although has an indefinite life, has been fully reserved for as realization of its benefit is unlikely.

The Company has net operating loss carry forwards of approximately \$270,555 and \$311,148 for Federal and State tax purposes respectively. These net operating loss carry forwards may be used to reduce federal and state taxable income and tax liabilities in future years and expire in various years through June 30, 2018 and June 30, 2010 for Federal and State tax purposes, respectively. In addition, the Company has Research and Development Tax Credits for State tax purposes of approximately \$9,829 which expires in various years through June 30, 2010.

The Company's provision for income taxes differs from applying the statutory U.S. federal income tax rate to the income before income taxes. The primary differences result from providing for state income taxes, generation of allowable tax credits and from deducting certain expenses for financial statement purposes but not for federal income tax purposes.

A reconciliation between taxes computed at the federal statutory rate and the consolidated effective tax rate follows:

	June 30,	
	2005	2004
Federal statutory tax rate	34.0%	34.0%
State income tax - net of federal tax benefit	3.2	6.0
R & D credits	-	(4.5)
Adjustment to prior year accrual for income tax	(8.2)	-
Adjustment in valuation allowance	-	20.9
Permanent and other differences	0.9	1.5
	29.9%	57.9%
	=====	=====

10. STOCK OPTIONS AND AWARDS

On January 22, 1998 the Board of Directors authorized two stock option plans effective July 1, 1998: one for the Chief Executive Officer (the "CEO") and an identical plan for senior management. Under the plans, the CEO, and separately, senior management, would be issued stock options, at the market price at the date of grant, in an amount equal to 3% of the incremental market cap of the Company divided by the stock price at June 30th in each of the next three years. The incremental market cap of the Company is defined as the number of outstanding shares at the end of each year multiplied by the increase in the market value per share for each year. These options would be equally divided by the number of participants in each plan.

Under these plans, 97,080 options at an exercise price of \$1 per share were granted on June 30, 1999, and 126,629 options at an exercise price of \$1.46 per share were granted on August 29, 2001 as of July 1, 2001. As of June 30, 2005, 105,524 options from the 2001 issuance remaining exercisable with an expiration of June 2006.

On August 29, 2001, the Board of Directors authorized two stock option plans effective July 1, 2001: one for the Chief Executive Officer and an identical plan for senior management. These plans were identical to the ones

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authorized on January 22, 1998 and effective July 1, 1998. No awards were made under these 2001 plans.

On January 22, 1998 the Board of Directors approved an option plan that granted each active director 5,000 common stock options annually. On October 21, 1998, 20,000 options were granted under this plan. The exercise price of \$0.75 was equal to the market value at the date of grant. These options expired on October 21, 2003 with 10,000 options exercised and 10,000 options expiring. On November 11, 1999, 25,000 stock options were granted under this plan at \$0.80 per share with an expiration of November 11, 2004 in which 20,000 options were exercised during fiscal year 2005.

On February 22, 2000 the option plan for directors was amended to award 2,000 options for each meeting attended, awarded at the annual meeting at the 5-day market price average. Under the amended plan, 62,000 options were awarded to the Board of Directors on October 24, 2000 at an exercise price of \$0.55, expiring October 23, 2005. On November 14, 2001 64,000 options were issued at an exercise price of \$1.11, expiring November 13, 2006. On November 13, 2002 80,000 options were issued at an exercise price of \$0.45, expiring November 13, 2007. 52,000 options were issued at an exercise price of \$1.10 on November 19, 2003 with an expiration of November 19, 2008. On November 17, 2004 56,000 options were issued to the Board of Directors at an exercise price of \$2.10, expiring November 17, 2009. There were no other stock option issuances during the 2004 and 2005 fiscal years.

On February 3, 2000 the Company issued 10,000 stock options to a senior executive as part of his employment contract. The options vested immediately and were priced at \$0.89 per share. These options were exercised prior to its February 3, 2005 expiration.

During the 2002 fiscal year, there were nine option grants for a total of 123,000 shares at exercise prices ranging from \$0.55 to \$1.15, as determined by their respective preceding 5-day market price average. These options vests 1/3 each year starting on the anniversary of the date of grant and expires in 5 years through May 21, 2007. 10,000 options were cancelled during fiscal 2003 due to the resignation of an optionee.

F-7

HYDROMER, INC. & SUBSIDIARY NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

A summary of activity under the plan for the years ending June 30, 2005 and 2004 is as follows:

	Common Stock Options Outstanding	
	Shares	Weighted Average Exercise Price
	-----	-----
Balance, June 30, 2003	534,244	\$ 0.93
Granted	52,000	1.10
Exercised	(10,000)	0.75
Canceled	(74,720)	0.97
	-----	-----
Balance, June 30, 2004	501,524	\$ 0.94
Granted	56,000	2.10

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Exercised	(30,000)	0.83
Canceled	(5,000)	0.80
	-----	-----
BALANCE, JUNE 30, 2005	522,524	\$ 1.08
	-----	-----

Following is a summary of the status of options outstanding as of June 30, 2005:

Exercise Price Range	Outstanding Options			Exercisable Options	
	Number	Weighted Average Remaining Contractual Life	Weighted Average Exercise Price	Number	Weighted Average Exercise Price
-----	-----	----	-----	-----	-----
\$0.45 - \$0.85	167,000	1.5 years	\$0.52	167,000	\$0.52
\$0.86 - \$1.68	299,524	1.6 years	\$1.20	299,524	\$1.20
\$1.69 - \$2.10	56,000	4.4 years	\$2.10	56,000	\$2.10
	-----	-----	-----	-----	-----
	522,524	1.9 years	\$1.08	522,524	\$1.08

PRO FORMA INFORMATION

The Company follows the disclosure only provisions of SFAS No. 123, ACCOUNTING FOR STOCK BASED COMPENSATION. Accordingly, no compensation expense has been recognized for stock options issued. Had compensation expense for the options which vested in 2005 and 2004 been determined based on the fair value at the grant date commensurate with the provisions of SFAS No. 123, the Company's net income and net income per share for 2005 and 2004, respectively, would have been reflected as to the pro forma amounts indicated below:

	2005	2004
	-----	-----
Net Income:		
As reported	\$269,251	\$231,336
Pro forma	209,396	198,610
Basic Income per Share:		
As reported	\$ 0.06	\$ 0.05
Pro forma	0.05	0.04

The fair value of each option grant is estimated on the date of grant using the Black-Scholes pricing model with the following weighted average assumptions for grants in 2005 and 2004, respectively: dividend yield of 0% and 0%; expected volatility of 115% and 170%; risk-free interest rate of 4.1% and 3.2%; and expected lives of 5 years in both years.

11. RETIREMENT PLAN

The Company sponsors a qualified 401(k) plan covering substantially all full time employees under which eligible employees can defer a portion of their annual compensation. The Company determines annually, the amount of matching contributions, which recently has been 25% on 6% of the employees' salary. The

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Company's matching contribution made to the plan during the years ended June 30, 2005 and 2004 were \$22,929 and \$17,000, respectively.

12. LEASES

There were no material non-cancelable lease terms in excess of one year as of June 30, 2005.

13. EARNINGS PER SHARE

The following table sets forth the computation of earnings per share and earnings per share - assuming dilution:

	2005	2004

Numerator:		
Net income	\$ 269,251	\$ 231,336
	=====	=====
Denominator:		
Denominator for earnings per share		
- weighted average shares outstanding	4,614,500	4,595,214
Effect of dilutive securities -		
stock options	167,000	467,191
	-----	-----
Denominator for earnings per		
share assuming dilution - adjusted		
weighted average shares outstanding	4,781,500	5,062,405
	=====	=====
Earnings per share	\$.06	\$.05
	=====	=====
Earnings per share - assuming dilution	\$.06	\$.05
	=====	=====

14. INDUSTRY SEGMENT INFORMATION

The Company operates two primary business segments: (1) Polymer Research and (2) Medical Products.

Products included in the polymer research segment are Aquadapt(R), Aquamere(R), Aquatrix(R), Dermaseal(R), Hydromer(R) Anti-Fog/Condensation Control Coatings, Hydromer(R) Lubricious Coatings, Sea-Slide(R) and T-Hexx(R) Barrier Dips and Sprays. Research and Development services and all of the Company's royalties, options and license revenues are reported in this segment.

The medical products segment includes an OEM product line of bipolar coagulation probes, jejunal, enteral and biliary catheters and stents, feeding accessories, guidewires, biofeedback devices for fecal and urinary incontinence and endoscopic accessories. Service revenues, including coating services and engineering services, are included in this segment.

Due to the multitude of products offered and the product gross margins, the Company does not track sales volumes by products.

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The Company operates globally in its segments with several large customers that are important to their operating results. One such customer accounted for 23% and 29% of the polymer research segment sales for the 2005 and 2004 fiscal years, respectively. For the medical products segment, four customers in the aggregate accounted for 57% and 71% of that segment's 2005 and 2004 sales, respectively.

The Company evaluates the segments by revenues, total expenses and earnings before income taxes. The Company's assets are not reviewed by business segment. The accounting policies of these segments are described in the summary of significant accounting policies.

F-8

HYDROMER, INC. & SUBSIDIARY NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

Corporate Overhead, primarily the salaries and fringes of senior management, support services (Accounting, Legal, Human Resources and Purchasing) and other shared services (Building maintenance and warehousing), is reflected separately from the results of the business segments in the following:

	Polymer Research	Medical Products*	Corporate Overhead	Total
	-----	-----	-----	-----

YEAR ENDED JUNE 30, 2005				
REVENUE	\$ 4,878,364	\$ 3,607,640		\$ 8,486,004
EXPENSES	(3,666,651)	(3,177,170)	\$ (1,262,867)	(8,106,688)
	-----	-----	-----	-----
EARNINGS (LOSS)				
BEFORE INCOME TAXES	\$ 1,211,713	\$ 430,470	\$ (1,262,867)	\$ 379,316
	=====	=====	=====	=====
Year Ended June 30, 2004				
Revenue	\$ 5,073,228	\$ 3,617,095		\$ 8,690,323
Expenses	(3,105,150)	(3,381,943)	\$ (1,402,375)	(7,889,468)
	-----	-----	-----	-----
Earnings (Loss)				
before Income Taxes	\$ 1,968,078	\$ 235,152	\$ (1,402,375)	\$ 800,855
	=====	=====	=====	=====

* Excludes the Fiscal 2004 Impairment of Goodwill for \$252,000 as such charge-off is not included in the periodic reporting segment evaluations.

Geographic revenues were as follows for the years ended June 30,

	2005	2004
	-----	-----
Domestic	84%	84%
Foreign	16%	16%

15. CONTINGENCIES

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Royalty revenues recorded by the Company's are based on the sales of licensee products as reported by the Company's licensees which has the risk of being under- or over-reported. To minimize such risks, the Company's management utilizes its knowledge and understanding of the licensee's business, the market and other pertinent factors in assessing the validity of reported royalties. In addition, the Company has a right to audit the amounts reported.

The Company has not received any claims by licensees for possible overpayment of royalties.

16. SUBSEQUENT EVENTS

In July 2005, the Company renewed its \$750,000 revolving line of credit agreement extending the maturity from November 30, 2005 to July 31, 2006.

In the first quarter of the 2005/2006 fiscal year the Company entered into two availability and supply agreements with former licensees of an expired patent. The first agreement required the client to purchase a minimum amount of product at \$100,000/year for the first year and a lower amount for the next four years. The second agreement carries a monthly availability fee of \$100,000 for three years at a favorable unit price. It can be terminated by the client upon a 90 day notice. Both contracts require the Company to escrow the formulas, in the event the Company can not supply the products.

F-9

INDEX TO EXHIBITS

3.a Certificate of Incorporation of the Company, as amended to date

3.b By-Laws of the Company, as amended to date

10.a Minutes of Meeting of the Board of Directors of the Company held on March 5, 1981 with respect to stock options granted to Manfred F. Dyck (Incorporated by reference to Exhibit 10.i to the Registration Statement).

10.b Agreement dated August 11, 1981 between Horizon Concepts, Inc., and the Company (Incorporated by reference to Exhibit 10.c to the Registration Statement).

10.c Agreement dated January 27, 1982 between Reliable Pharmaceutical Company, Inc. and the Company (Incorporated by reference to Exhibit 10.d to the Registration Statement).

10.d License Agreement dated July 14, 1982 between Biosearch Medical Products Inc. and the Company (Incorporated by reference to Exhibit 10.g to the Registration Statement).

10.e Management Services Agreement dated July 14, 1982 between Biosearch Medical Products Inc. and the Company (Incorporated by reference to Exhibit 10.h to the Registration Statement).

10.f Amendment dated October 7, 1982 to Agreement dated January 27, 1982 between Reliable Pharmaceutical Company, Inc. and the Company, together with letter dated October 14, 1982 from Reliable Pharmaceutical Company, Inc. to the Company (Incorporated by reference to Exhibit 10.f to the 1983 Annual Report).

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10.g Hydromer Coating agreement dated February 11, 1983 between Pacesetter Systems, Inc. and the Company (Incorporated by reference to Exhibit 10.g to the 1983 Annual Report).

10.h Lease Agreement dated April 5, 1983 between Salem Realty and the Company (Incorporated by reference to Exhibit 10.h to the 1983 Annual Report).

10.i License Agreement dated April 25, 1983 between CardioSearch Inc. and the Company (Incorporated by reference to Exhibit 10.i to the 1983 Annual Report).

10.j Trademark License Agreement dated April 25, 1983 between CardioSearch Inc. and the Company (Incorporated by reference to Exhibit 10.j to the 1983 Annual Report).

10.k Agreement dated August 31, 1983 between Becton, Dickinson & Company and the Company (Incorporated by reference to Exhibit 10.l to the 1983 Annual Report).

10.l Current Report on Form 8-K filed May 30, 1986

10.m Hydromer Coating License Agreement dated September 30, 1984 between Axiom Medical, Inc. and the Company (Incorporated by reference to Exhibit 10.m to the 1984 Annual Report).

10.n 1982 Stock Option Plan of the Company (Incorporated by reference to Exhibit 10.m to the 1983 Annual Report).

10.o Amendment dated June 26, 1984 to Agreement dated August 3, 1983 between Becton, Dickinson & Company and the Company (Incorporated by reference to Exhibit 10.o to the 1984 Annual Report).

10.p License Agreement dated July 31, 1984 between Kendall Company and the Company (Incorporated by reference to Exhibit 10.p to the 1984 Annual Report).

10.q License Agreement dated March 1, 1985 between Van-Tec Inc. and the Company and Letter of Amendment thereto dated June 13, 1985 (Incorporated by reference to Exhibit 10.o to the 1985 Annual Report).

10.r Telex dated June 24, 1985 terminating License Agreement with CardioSearch Inc. (Incorporated by reference to Exhibit 10.p to the 1984 Annual Report).

10.s Amendment dated as of December 31, 1984 to Management Services Agreement dated July 14, 1982 between Biosearch Medical Products Inc. and the Company (Incorporated by reference to Exhibit 10.q to the 1985 Annual Report).

10.t Lease Renewal Agreement dated April 15, 1985 between Salem Realty and the Company (Incorporated by reference to Exhibit 10.r to the 1985 Annual Report).

10.u Lease Agreement dated December 4, 1984 between Biosearch Medical Products Inc. and the Company (Incorporated by reference to Exhibit 10.s to the 1985 Annual Report).

10.v License Agreement dated April 11, 1986 between Axiom Medical, Inc. and the Company (Incorporated by reference to Exhibit 10.i to the 1986 Annual Report).

10.w License Agreement dated September 13, 1985 between U. S. Viggo and the Company (Incorporated by reference to Exhibit 10.c to the 1986 Annual

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Report).

10.x License Agreement dated March 27, 1986 between Wilkinson Sword Limited and the Company (Incorporated by reference to Exhibit 10.f of the 1986 Annual Report).

10.y Lease Renewal Agreement dated April 15, 1987 between Salem Realty and the Company (Incorporated by reference to Exhibit 10.y to the 1987 Annual Report).

10.z License Agreement dated April 30, 1986 between HPK International and the Company (Incorporated by reference to Exhibit 10.j to the 1986 Annual Report).

10.aa License Agreement dated August 1, 1986 between Film Specialties, Inc. and the Company (Incorporated by reference to Exhibit 10.aa to the 1987 Annual Report).

10.ab Lease Renewal Agreement dated April 15, 1988 between Salem Realty and the Company (Incorporated by reference to Exhibit 10.ab to the 1988 Annual Report).

10.ac License Agreement dated June 30, 1987 between Richards Medical Company and the Company (Incorporated by reference to Exhibit 10.ac to the 1988 Annual Report).

10.ad License Agreement dated December 1, 1987 between Mallinckrodt, Inc. and the Company (Incorporated by reference to Exhibit 10.ad to the 1988 Annual Report).

10.ae Option Agreement dated January 28, 1988 between Cordis Corporation and the Company (Incorporated by reference to Exhibit 10.ae to the 1988 Annual Report).

10.af Lease Agreement dated April 15, 1988 between Biosearch Medical Products Inc. and the Company (Incorporated by reference to Exhibit 10.ag of the 1988 Annual Report).

10.ag Letters dated June 11, 1987 and September 22, 1987 to U. S. Viggo, Inc. modifying License Agreement dated September 13, 1985, to cover only central venous catheters (Incorporated by reference to Exhibit 10.ag to the 1988 Annual Report).

10.ah Lease Renewal Agreement dated April 15, 1989 between Salem Realty and the Company (Incorporated by reference to Exhibit 10.ah to the 1989 Annual Report).

10.ai Amendment dated October 1, 1988 to License Agreement dated September 13, 1985, between U. S. Viggo and the Company (Incorporated by reference to Exhibit 10.ai to the 1989 Annual Report).

10.aj License Agreement dated October 20, 1988 between Cordis Corp. and the Company (Incorporated by reference to Exhibit 10.aj to the 1989 Annual Report).

10.ak License Agreement dated March 31, 1989 between Cathlab Corp. and the Company (Incorporated by reference to Exhibit 10.ak to the 1989 Annual Report).

10.al Amendment dated December 1, 1988 to License Agreement dated August

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1, 1986 between Film Specialties, Inc. and the Company (Incorporated by reference to Exhibit 10.al to the 1989 Annual Report).

10.am Finders Agreement dated August 20, 1987 between Phoenix Chemical, Inc. and the Company (Incorporated by reference to Exhibit 10.am to the 1989 Annual Report).

10.an License Agreement dated September 10, 1989 between the Stent Division of Schneider and the Company (Incorporated by reference to Exhibit 10.an to the 1990 Annual Report).

10.ao License Agreement dated March 30, 1990 between Cosmo Ikko Company and the Company (Incorporated by reference to Exhibit 10.ao to the 1990 Annual Report).

10.ap License Agreement dated April 12, 1990 between Interventional Therapeutics, Inc. and the Company and amendment dated May 7, 1990 to the Agreement dated April 12, 1990 between Interventional Therapeutics, Inc. and the Company (Incorporated by reference to Exhibit 10.ap to the 1990 Annual Report).

10.aq Amended License Agreement dated January 1, 1990 between the Wilkinson Sword group of companies and the Company (Incorporated by reference to Exhibit 10.aq the 1990 Annual Report).

10.ar Lease Agreement dated April 15, 1990 between Salem Realty and the Company (Incorporated by reference to Exhibit 10.ar to the 1990 Annual Report).

10.as Amendment to the Agreement dated July 31, 1984 between Kendall Company and the Company (Incorporated by reference to Exhibit 10.as to the 1990 Annual Report).

10.at License Agreement dated January 11, 1991 between Biosearch Medical Products Inc. and the Company (Incorporated by reference to Exhibit 10.at to the 1991 Annual Report).

10.au License Agreement dated May 16, 1991 between I E Sensors and the Company (Incorporated by reference to Exhibit 10.au to the 1991 Annual Report).

10.av Lease Renewal Agreement dated April 15, 1991 between Salem Realty and The Company (Incorporated by reference to Exhibit 10.av to the 1991 Annual Report).

10.aw License Agreement dated July 25, 1991 between Johnson & Johnson Orthopaedics and the Company (Incorporated by reference to Exhibit 10.aw to the 1992 Annual Report).

10.ax License Agreement dated August 19, 1991 between Navarre Laboratories Ltd. and the Company (Incorporated by reference to Exhibit 10.ax to the 1992 Annual Report).

10.ay Amended License Agreement dated September 15, 1991 between Boston Scientific Corp. and the Company (Incorporated by reference to Exhibit 10.ay to the 1992 Annual Report).

10.az Option/License Agreement dated September 23, 1991 between Elan Corp. PLC and the Company (Incorporated by reference to Exhibit 10.az to the 1992 Annual Report).

10.ba Lease Agreement dated November 1, 1991 between Morton Street Realty and the Company (Incorporated by reference to Exhibit 10.ba to the 1992

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Annual Report).

10.bb License Agreement dated August 17, 1992 between SCIMED Peripheral Interventions, division of SCIMED Life Systems, Inc. and the Company. (Incorporated by reference to Exhibit 10.bb to the 1993 Annual Report).

10.bc License Agreement dated March 9, 1993 between Arrow International, Inc. and the Company. (Incorporated by reference to Exhibit 10.bc to the 1993 Annual Report).

10.bd License Agreement dated April 28, 1993 between St. Jude Medical, Inc. and the Company. (Incorporated by reference to Exhibit 10.bd to the 1993 Annual Report).

10.be License Agreement dated November 11, 1993 between Katoh Hatsujyo Kaisha, Ltd. and the Company. (Incorporated by reference to Exhibit 10.be to the 1994 Annual Report).

10.bf Lease Agreement dated June 9, 1995 between Salem Realty and the Company (Incorporated by reference to Exhibit 10.bf to the 1995 Annual Report).

10.bg Amendment dated September 20, 1995 to License Agreement dated April 28, 1993 between St. Jude Medical, Inc. and the Company. (Incorporated by reference to Exhibit 10.bg to the 1996 Annual Report).

10.bh License Agreement dated April 12, 1990 between Interventional Therapeutics and the Company was terminated effective December 22, 1995. (Incorporated by reference to Exhibit 10.bh to the 1996 Annual Report).

10.bi License Agreement dated May 16, 1991 between I E Sensors and the Company was terminated effective December 31, 1995. (Incorporated by reference to Exhibit 10.bi to the 1996 Annual Report).

10.bj Consented to the assignment of license agreement dated April 28, 1993 between St. Jude Medical, Inc. and the Company to CR Bard dated January 18, 1996. (Incorporated by reference to Exhibit 10.bj to the 1996 Annual Report).

10.bk License Agreement dated April 30, 1986 between HPK International and the Company was terminated effective February 19, 1996. (Incorporated by reference to Exhibit 10.bk to the 1996 Annual Report).

10.bl License Agreement dated June 6, 1996 between Biosearch Medical Products Inc. and the Company. (Incorporated by reference to Exhibit 10.bl to the 1996 Annual Report).

10.bm License Agreement dated August 1, 1996 between Biosearch Medical Products Inc. and the Company.

10.bn Amended License Agreement dated September 4, 1996 between SCIMED (Boston Scientific Corporation) and the Company.

10.bo License Agreement dated January 6, 1997 between Sherwood Davis & Geck and the Company.

10.bp Use permit for certain designated area dated May 4, 1997 between Biosearch Medical Products Inc. and the Company

10.bq Contract of sale between Biosearch Medical Products and the Company for the sale of 35 Industrial Parkway dated 3/31/98

10.br Note and mortgage with PNC Bank dated 6/12/98

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- 10.bs 3 year lease agreement with Biosearch Medical Products dated 6/12/98 for 35 Industrial Parkway
- 10.bt License of technology, supply and stock purchase agreement with C.R.Bard dated 2/25/99
- 10.bu Trademark and technology license agreement with AST dated 3/9/99
- 10.bv License of two gel patents from Ridge Scientific dated 11/1/98
- 10.bw License and Supply agreement with Gallini SRL dated 6/28/00
- 10.bx Standstill agreement with license option with IMED Pharma Inc. dated 3/30/00
- 10.by License of technology with Symbiotech Medical Inc. dated 3/28/00
- 10.bz License and supply agreement with TP Orthodontics Inc. dated 3/30/00
- 10.ca License Agreement dated July 1, 2000 between Becton Dickinson and Company, Inc. and the Company.
- 10.cb License Agreement dated January 1, 2001 between LHS Limited and LHS Holding Limited, English dba KLEENCARE and the Company.
- 10.cc License Agreement dated April 17, 2001 between Tyco Healthcare Group LP and the Company.
- 10.cd Construction Contract dated April 19, 2001 between REDCO Engineering & Construction Corp and the Company.
- 10.ce Service Agreement dated April 23, 2001 between Tyco Healthcare Group LP and the Company.
- 10.cf Loan Agreement dated June 7, 2001 between New Millenium Bank and the Company.
- 10.cg By-Laws Articles of Incorporation.
- 10.ch Loan Agreement dated June 30, 2005 between Wachovia Bank, N.A. and the Company.
24. Power of Attorney (see "Power of Attorney" in the Annual Report on Form 10-KSB).
- 31.1 Certification of Manfred F. Dyck, Chief Executive Officer, pursuant to Securities Exchange Act Rule 13a-14(a).
- 31.2 Certification of Robert Y. Lee, Chief Financial Officer, pursuant to Securities Exchange Act Rule 13a-14(a).
- 32.1 Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, signed by Manfred F. Dyck, Chief Executive Officer of Hydromer, Inc.
- 32.2 Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, signed by Robert Y. Lee, Chief Financial Officer of Hydromer, Inc.

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INDEX TO 2005 10-KSB CERTIFICATIONS

Exhibit No.	Description
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32.2

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