WATER CHEF INC
Form 10KSB
March 30, 2007

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

FORM 10-KSB
(Mark One)

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

For the Year Ended December 31, 2006

OR

[ ] TRANSITION REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from to

Commission file number: 0-30544

WATER CHEF, INC
(Name of small business issuer in its charter)

DELAWARE	86-0515678
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

1007 GLEN COVE AVENUE, SUITE 1
GLEN HEAD, NY 11545
(Address of principal executive offices) (Zip Code)

(516) 656-0059
(Issuer's telephone number)

Securities registered under section 12(b) of the Exchange Act: None.

Securities registered under section 12 (g) of the Exchange Act: Common stock, Par value $.001

Redeemable Common Stock Purchase Warrants.

Check whether the issuer is not required to file reports pursuant to Section 13 or 15(d) of the Exchange Act. |_|

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

Check if there is no disclosure of delinquent filers in response to Item 405 of Regulation S-B is 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. |_|

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes |_| No |X|

The issuer's net sales for the most recent fiscal year were $115,000.

The aggregate market value of the voting stock held by non-affiliates based upon the last sale price on March 15, 2007 was approximately $ 21,140,962.

As of March 26, 2007, the Registrant had 180,040,087 shares of its Common Stock, $0.001 par value, outstanding.

DOCUMENTS INCORPORATED BY REFERENCE None

Transitional Small Business Disclosure Format (Check one): Yes |_| No |X|

WATER CHEF, INC.
ANNUAL REPORT ON FORM 10-KSB

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ITEM 1. DESCRIPTION OF BUSINESS

THE COMPANY

Water Chef, Inc. (the "Company," "Water Chef"), designs and markets water purification equipment. Water coolers and filters were a substantial part of the Company's business from 1993 until the fourth quarter of 2001, at which time this business was sold so that Water Chef could concentrate on the further development, manufacturing, and marketing of their patented line of "PureSafe" water purification systems. The accompanying financial statements have been prepared assuming the Company will continue as a going concern. To date, the Company has shipped 26 PureSafe units. Revenue has been recognized on only 8 PureSafe units, as 18 units that were shipped to the Kingdom of Jordan have not met the criteria for revenue recognition due to no reasonable assurance of collectibility. In addition, the Company received deposits in 2005 for two units that were shipped in 2006.

BACKGROUND

The Company was originally incorporated under Arizona law in 1985 and merged into a Delaware corporation in 1987. In 1993, the Company, then known as Auto Swap, U.S.A., entered into a reverse merger with Water Chef, Inc., a Nevada corporation, which manufactured and marketed water coolers and filters.

PRODUCTS

In 2001 the Company decided to concentrate its efforts on the further development, manufacturing and marketing of the PureSafe Water Station (the "PureSafe"), because although Water Chef believed that its water dispensers and its wide variety of consumer oriented water filtration products met or exceeded the design, quality and performance of competitive products, market considerations were such as to limit the opportunities for profit and growth.

In 1998, searching for a "killer application," Water Chef management focused on the worldwide need for safe drinking water for populations who are not served by municipal water treatment facilities, or are served by municipal systems that have malfunctioned because of improper maintenance or faulty design. The result of that activity is the PureSafe Water Station, a turn-key unit that converts "gray," or bathing grade, water into EPA grade drinking water. The PureSafe eliminates all living pathogens that pollute non-processed water - bacteria, cysts, viruses, parasites, etc. - at an affordable cost for the emerging economies of the world.

The PureSafe was tested by H2M Labs, Inc. which has been approved by Nassau and Suffolk counties in New York to perform drinking water testing for the various municipalities in those counties. The specific test performed was a total and fecal coliform bacteria test, wherein the source water storage tank which feeds the PureSafe was tested for the presence of total and fecal coliform bacteria. The source water tank was found to have 50 colonies of coliform bacteria present. The source water tank was then "spiked" with a three (3) liter concentration of laboratory grown and cultured bacteria and the storage tank was measured again with 80,000,000 colonies of bacteria detected. After being

processed through the PureSafe system, the water was tested again, and "FEWER THAN 2 COLONIES" were detected. In addition to the laboratory test conducted for Water Chef by H2M Labs, the available scientific literature, in industry journals such as Water Technology and Water Conditioning and Purification International, supports the statement that an ozone system such as the one utilized in the PureSafe effectively eliminates all living pathogens. Ozone was first used in municipal water treatment in Nice, France in 1904, and then in the Jerome Park Reservoir in the Bronx, New York in 1906.

The PureSafe is a self-contained, six stage water purification center. It is housed in the equivalent of a small storage container - approximately four feet wide, seven feet long, and six and one-half feet high. The unit weighs approximately eleven hundred pounds (without water) and has been configured for portability, durability, and easy access to its essentially off-the-shelf components. It is constructed with weather and UV resistant fiberglass, aluminum and steel, and is equipped with internal and external lighting.

The core version of the PureSafe can purify and dispense up to 15,000 gallons of water per day for an all-inclusive cost (labor, power, amortization of the capital cost, replacement filters, cartridges and media) of approximately one-half cent per gallon. The process wastes very little water, producing approximately one gallon of pure drinking water for every gallon processed. The unit can be moved with a single fork-lift and is transportable by truck or helicopter. Operating the PureSafe is simple and straightforward. Due to its turn-key design, minimum wage personnel can be trained to operate the unit. A system of fail-safes is built into the operation, and aside from easily installable spares such as filters and cartridges, a maintenance and oversight program established by Water Chef should maintain the operating efficiencies built into the system. Water Chef warrants each unit for a period of one year so long as the consumer adheres to required maintenance protocols, using Water Chef supplied parts, as prescribed in the maintenance manual. The Company also offers larger stand-alone versions of the PureSafe to provide pure water in quantities up to 20,000 gallons per hour. To date, there have been no warranty claims for the PureSafe product operating in the field.

While each unit is configured to respond to the particular water quality of a particular site, such as arsenic removal, seawater desalination, oil separation, etc., the typical unit contains the following components:

a. Inlet connection with macro-filter - designed to strain the input water, removes large particulates and directs water into the system 2 PRODUCTS (continued)

b. Inlet pump - self-priming pump which maintains water pressure at minimum 40 p.s.i. throughout the system

c. Pre-depth media filter - a multi-media mixed bed to remove pollutants. Pressure gauges mounted on the exterior front panel of the unit allow for visible monitoring of system performance.

d. Ozone generator - provides a rich ozone source that effectively kills all living pathogens such as bacteria, viruses, cysts, parasites, etc. Unused ozone reverts to oxygen and produces no harmful byproducts.

e. Ozone mixing tank - Water Chef's proprietary process for effectively mixing the ozone into the water and maintaining the required contact time to ensure oxidation of contaminants.

f. Process pump - provides optimal operation of the ozone processing.

g. Post-depth media filter - another, different, multi-media mixed bed designed to filter out oxidized or precipitated pollutants and contaminants after the ozone treatment. Effectively removes metals, organics and inorganics. Pressure gauges on the front panel indicate the need for backwashing to maintain optimal performance.

h. Ultraviolet treatment - provided by a UV lamp as a redundant sterilizer step to eliminate any surviving pathogens or micro-organisms. The UV lamp is tuned to a frequency which also converts O_3 (ozone) back to O_2 (oxygen).

i. KDF filter - an ion exchange media containing a proprietary blend of copper, zinc and other alloys, effectively absorbs chlorine and biological, inorganic and metallic contaminants.

j. Carbon filter - prevents bacteria re-growth while removing inorganic compounds and improves water taste and removes odor. The carbon filter also acts as a redundant ozone destruct mechanism.

k. Mixer - sends ozone treated water to the bottle washing stations.

l. Bottle washing stations - incorporated on the outside front of the unit for easy access in order to effectively clean bottles used to carry water treated at the site.

m. Dispensing stations - four individual dispensing lines, each with flow adjusting valves to help regulate a smooth, steady flow of water into clean bottles.

MANUFACTURING

In 2000, the Company entered into a subcontracting agreement with Davis Aircraft Products Inc, ("Davis") for the manufacture of the PureSafe. Based upon the experience and the resources of Davis, Water Chef's management believes that Davis can provide the production and manufacturing support services necessary to supply Water Chef's requirements over the foreseeable future at a price, and with the quality and performance standards necessary to meet, or exceed, the needs of the markets that the Company expects to serve. In addition, Davis supervises much of the Company's research and development activities.

RAW MATERIALS

The PureSafe has been designed to use, for the most part, readily available off-the-shelf components, sub-systems and equipment. Inasmuch as each of the components and sub-systems are available from multiple vendors, the Company does not believe that obtaining these for its sub-contractor, for itself, or for others if it chooses to manufacture elsewhere, will be a problem.

COMPETITION

Water Chef's modular, turn-key PureSafe Water Station directly addresses the drinking water needs of those environs which do not today, and are unlikely to enjoy access to municipally treated water. The Company has produced a turnkey solution that produces pure water to meet U.S. EPA drinking water standards. This is a far different market than that addressed by the segment of the industry which has concentrated on the multi-billion dollar municipal water treatment sector, or the equally large residential sector. The municipal solution requires significant investment for infrastructure development (building plants and laying miles of distribution pipes), and products for residential markets do not offer the performance or features to meet the needs

of the underdeveloped nations of the world.

COMPETITION (continued)

Management does recognize that its potential competitors have far more resources, and that being first to the marketplace is no assurance of success. It must be assumed that others are working on systems that, if successfully brought to market, could seriously impact the viability of the Company.

The Company currently has contracts to sell PureSafe units in Laos and China. In addition, the Company is actively marketing its products to potential customers in Bangladesh, China, Peru, Egypt, India and Honduras, and to agencies and departments of the U.S. Government.

MARKETING

The potential market for the PureSafe is substantial and is both worldwide and domestic. According to studies performed by the World Health Organization (WHO) and the United Nations, major parts of Africa, the Middle East, Southeast Asia, the Indian sub-continent, Latin and South America, the Caribbean, and much of Eastern Europe is in need of adequate supplies of pure water. Parts of Florida, Georgia, and other regions in the United States have also reported fresh water deficits. In part, solving this problem has been a question of appropriate technology. Secondarily, but just as important, in a vast part of the world is the need to secure third party financing so that the local populace can enjoy the benefits of clean water.

Water Chef believes that it has demonstrated that it possesses the technology. The Company also believes that financing is available for third world economies from a variety of sources. The challenge for the Company, a virtual unknown in the industry and with limited capital, is getting its message in front of decision makers. To this end, Water Chef has enlisted the aid of some of the world's most outstanding experts in water purification, especially as it relates to the needs of underdeveloped countries.

The Company's Scientific Advisory Board is chaired by Dr. Ronald Hart, former Director of The National Center for Toxicological Research and a U.S. Food and Drug Administration "Distinguished Scientist in Residence." The Board also includes Dr. Mohamed M. Salem, Professor of Occupational and Environmental Medicine, Cairo University; Dr. Richard Wilson, Mallinckrodt Research Professor of Physics, Harvard University; and Dr. Mostafa K. Tolba, former Under-Secretary-General of the United Nations and Director of the U.N.'s Environmental Program.

Not only have the members of the Scientific Advisory Board provided valuable input and guidance to the Company with respect to system design, technological input, remediation approaches and a great deal of information relative to the unique water problems facing many areas of the world, but they have also been active in introducing Water Chef to commercial opportunities

During 2004, Water Chef established a relationship with the International Multiracial Shared Cultural Organization (IMSCO), an NGO (non-governmental organization) specialized with the Economic and Social Council of the United Nations. As a result of this relationship Water Chef has received United Nations certification for its pure water humanitarian projects in Honduras and Bangladesh, and became eligible to apply for third party funding of these projects. As of year-end 2004, the Company has submitted these projects for

funding approval, but has received no assurance of funding.

In September 2006, WaterChef appointed The Marshall Group as exclusive sales representative of the Company's products for India. With the pure water demands of its growing middle class and with increased attention being placed on the contamination of India's ground and surface water resources, the Company believes that the Indian market for its products is extremely attractive.

PATENTS

The Company filed for patent protection on its PureSafe Water Station in October of 1998 and received formal notification that the patent had been issued on February 19, 2002. The Company feels that this patent upholds its claims that the PureSafe system is a unique product. In addition to its U.S. patent, the Company has filed for patent protection in the countries of the European Union, and in Canada, Mexico, China, Hong Kong, Korea and Japan. The patent application for the European Union (01-126 980.0) was filed on November 13, 2001; Canadian Application No. 2,362,107 was filed on November 3, 2001; Mexican Application No. PA/a/2001/12042 was filed on November 23, 2001;the Chinese Application No. 01136187.5 was filed on November 21, 2001, and was found to be in compliance on June 20, 2003; the Hong Kong Application No. 03107837.9 was filed on October 3, 2003; and the Korean Patent Application No. 10-2001-0070453 was filed on November 20, 2001. Each of the patent applications has been accepted, Requests for Examination have been made, and the Company currently has patent protection in the requested venues. In January 2006, the Chinese State Intellectual Property Office granted the patent rights for the invention, and, in September 2006, WaterChef was advised by patent counsel that the European Patent Office had decided to grant our patent for the European Union.

PATENTS (continued)

The name PureSafe Water Station and the stylized water droplet mark have been trademarked in the United States.

Water Chef has also incorporated patented and proprietary technology in the PureSafe and is confident that it can protect this intellectual capital throughout the manufacturing and distribution cycle.

There can be no assurance that any application of the Company's technologies will not infringe patent or proprietary rights of others, or that licenses which might be required for the Company's processes or products would be available on favorable terms. Furthermore, there can be no assurance that challenges will not be made against the validity of the Company's patent, or that defenses instituted to protect against patent violation will be successful.

SEASONALITY

The Company does not expect the Pure Safe to be influenced by seasonality.

GOVERNMENT APPROVALS

The Company's marketing efforts to date have been directed to Central and South America, the Asian sub-continent, China and the Middle East. No specific government approvals are required, except for the possibility that export licenses will be required in specific instances.

RESEARCH AND DEVELOPMENT

Research and development takes place at the Company's office. Testing, modeling, simulation and prototype manufacturing are outsourced, with much of the ongoing development taking place at the Company's contract manufacturing facilities under the supervision of Davis Water Products. The Company estimates to date that the design, prototyping, development and marketing of the PureSafe Water Station has cost in excess of $2 million.

INSURANCE

The Company maintains Directors' and Officers' Insurance in the aggregate amount of $2,000,000, and a $2,000,000 general business liability policy. The Company believes its insurance coverage to be adequate.

EMPLOYEES

As of December 31, 2006, the Company employed one executive officer and one administrative employee in its headquarters.

The Company believes there are a sufficient number of persons available at prevailing wage rates in or near our manufacturing locations that should expansion of its production require additional employees, they would be readily available. The Company has no collective bargaining agreement with any of its employees.

ITEM 2. DESCRIPTION OF PROPERTY

The Company presently has no owned or leased manufacturing facilities, nor does the Company have a plan to acquire its own manufacturing facility. The PureSafe Water Station is manufactured for the Company under a contract by Davis Water Products.

The Company maintains its principal place of business at 1007 Glen Cove Avenue, Suite 1, Glen Head, New York 11545. The company leases 1,100 square feet in such building at $2,731 per month on a month-to-month basis.

To the extent possible, the Company intends to utilize leased space for its future needs.

ITEM 3. LEGAL PROCEEDINGS

On July 14, 2006, Funding Group, Inc. filed a complaint with the Supreme Court of the State of New York in New York County seeking damages due to an alleged breach of contract related to a $25,000 loan made by the plaintiff to the Company. On October 11, 2006, the Company filed a counter claim against Funding Group, Inc. with the Supreme Court of the State of New York. The Company believes the complaint is without merit and intends to vigorously defend itself in these actions, and believes that the eventual outcome of these matters will not have a material adverse effect on the Company. However, the ultimate outcome of these matters cannot be determined at this time.

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

Not Applicable

PART II

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

PRICE RANGE OF COMMON STOCK

The Company's common stock is traded on the Over-The-Counter Electronic Bulletin Board ("OTCBB") under the symbol WTER.OB. This market is categorized as being "thin" which means that there is generally a paucity of buyers and sellers as found in the more heavily traded Small Cap and NASDAQ markets. OTCBB stocks generally do not have the trading characteristics of more seasoned companies as they lack the market-makers that will make orderly markets as well as the buyers and sellers that give depth, liquidity and orderliness to those markets. In addition, the solicitation of orders and/or the recommendations for purchase of OTCBB stocks is restricted in many cases by the National Association of Securities Dealers and by individual brokerage firms as well.

The chart below sets forth the range of high and low bid prices for the Company's common stock based on high and low bid prices during each specified period as reported by the National Quotation Bureau, Inc. The prices reflect inter-dealer prices without retail mark-up, markdown, quotation or commission and do not necessarily represent actual transactions.

	HIGH	LOW
2005		
First Quarter	.28	.14
Second Quarter	.21	.11
Third Quarter	.29	.13
Fourth Quarter	.17	.06
2006		
First Quarter	.19	.07
Second Quarter	.23	.10
Third Quarter	.13	.09
Fourth Quarter	.15	.07

As of the close of business on December 31, 2006, there were 836 common stock holders of record.

DIVIDENDS

We have not paid any cash dividends on our common stock since our inception and do not anticipate paying any cash dividends in the foreseeable future. We plan to retain our earnings, if any, to provide funds for the expansion of our business. Subject to our obligations to the holders of our Series A and Series D Preferred shares, and to the holders of our Series F convertible preferred stock, the holders of our common stock are entitled to dividends when and if declared by our Board of Directors from legally available funds. Our Board of Directors will determine future dividend policy based upon conditions at that point, including our earnings and financial condition, capital requirements and other relevant factors.

EQUITY COMPENSATION PLAN INFORMATION

The following table provides information as of December 31, 2006 with respect to our shares of Common Stock that may be issued under our existing equity compensation plans:

Plan Category	(a) Number of securities to be issued upon exercise of Outstanding options, warrants, and rights	(Weig ave exercis of outs opti warr and r
Equity compensation plans approved by security holders	--	-
Equity compensation plans not approved by security Holders:		
Stock option plans (2)	5,000,000	$0

(1) Excludes securities listed in column (a)

(2) Consists of 5,000,000 stock appreciation rights granted to David A. Conway that vest over 5 years.

On January 29, 2007, David A. Conway resigned as President and Chief Executive Officer and surrendered his Stock Appreciation Rights to the Company.

RECENT ISSUANCES OF UNREGISTERED SECURITIES

None issued during 4th Quarter ended December 31, 2006.

ITEM 6. MANAGEMENT'S DISCUSSION AND ANALYSIS OR PLAN OF OPERATION.

INTRODUCTION

DEVELOPMENT OF THE COMPANY

The Company was originally incorporated under Arizona law in 1985 and merged into a Delaware corporation in 1987. In 1993, the Company, then known as Auto Swap, U.S.A., entered into a reverse merger with Water Chef, Inc., a Nevada corporation that manufactured and marketed water coolers and filters.

The PureSafe has been designed by the Company to meet the needs of communities who either did not have access to municipal water treatment systems, or of those whose systems had been compromised, either by environmental factors or by faulty design or maintenance.

Off-Balance Sheet Arrangements

We do not have any off-balance sheet debt nor did we have any transactions, arrangements, obligations (including contingent obligations) or other relationships with any entities or other persons that may have a material current or future effect on financial conditions, changes in financial conditions, result of operations, liquidity, capital expenditures, capital

resources, or significant components of revenue or expenses.

RESULTS OF OPERATIONS

Sales for the years ended December 31, 2006 and 2005 were $115,000 and $260,000, respectively. During the year ended December 31, 2006, the Company recognized the sale of two PureSafe Water Station Systems.

Cost of sales increased from $42,000 for the year ended December 31, 2005, to $114,000 for the year ended December 31, 2006, an increase of $72,000, or 171%. An analysis of the components of cost of sales follows:

Cost of Sales Period	Product CGS	Rent and Overhead Payments to Manufacturer	Total Cost of Sales
2006	$30,000	$84,000	$114,000
2005	$ --	$42,000	$ 42,000

Selling, general and administrative expenses for the year ended December 31, 2006 were $1,559,464 compared to $1,194,577 for the year ended December 31, 2005, an increase of $364,887 or 31%.

Interest expense for the year ended December 31, 2006 was $380,553 compared to $244,191 for the year ended December 31, 2005, an increase of $136,362.

The net loss for the year ended December 31, 2006 was $2,072,917 compared to $1,168,328 for the year ended December 31, 2005, an increase of $904,589.

LIQUIDITY AND CAPITAL RESOURCES

At December 31, 2006, the Company had a stockholders' deficiency of $3,625,706 and a working capital deficiency of $3,123,220. In addition, the Company has a net loss of $2,072,917 and $1,168,328 for the years ended December 31, 2006 and 2005, respectively. The financial statements have been prepared assuming that the Company will continue as a going concern. The Independent Registered Public Accounting Firm's report on its financial statements included elsewhere herein contains an explanatory paragraph about conditions that raise substantial doubt about the Company's ability to continue as a going concern. Management's plans with respect to these matters include restructuring its existing debt and raising additional capital through future issuances of stock and/or debt. The financial statements do not include any adjustments that might be necessary should the Company be unable to continue as a going concern.

In October 2006, the Company entered into a loan agreement with Southridge Partners LP, pursuant to which the Company received a convertible loan of $300,000, less legal fees, secured by four million shares of the Company's common stock owned by the former President and Chief Executive Officer. The loan principal and interest was due and payable, in cash or shares of common stock, in February 2007.

Under the terms of the note, the Company is currently in default. Subsequent to the year end, the Company issued 948,670 shares of common stock for the settlement of $100,000 of principal and $3,249 of accrued interest. The Company plans to issue additional shares of common stock under the terms of the note for the settlement of the remaining principal and accrued interest.

The Company, during 2006 and 2005, raised $568,000 and $494,960, respectively,

through the sale of its common and preferred stock.

Water Chef was a defendant in a legal action brought by certain debenture holders ("Bridge Loans") in New Hampshire Superior Court seeking repayment of debenture principal of $300,000 and accrued interest from 1997. On June 22, 2002 a settlement was reached whereby the Company agreed to (i) issue a minimum of 3,000,000 shares of common stock valued at $497,500 in lieu of the principal and interest owed to the debenture holders who participated in this legal action. The Company recorded the debentures at $300,000, plus accrued interest of $39,400, for a total of $339,400. The difference between the $497,500, the value for the 3,000,000 shares, divided by the average daily trading price for the 30 days subsequent to the settlement, was greater than the original 3,000,000 shares. Due to these requirements, the Company was obligated to issue an additional 14,037,671 shares. As of December 31, 2004, the Company has issued the 3,000,000 shares and the additional 14,037,671 shares originally valued at $497,500. Attached to the original Bridge Loans were warrants for the purchase of 1,666,667 shares of the Company's common stock at $0.15 per share. The debenture holders that participated in the legal action had the lives of their warrants extended from March 2002 to March 2004. In connection with the issuance of the Bridge Lenders' shares the Company further extended the expiration date of the warrants to a date twelve months after the effective date of the Registration Statement filed with the Securities and Exchange Commission on January 24, 2005 which was declared effective by the Securities and Exchange Commission on June 7, 2005. The warrants expired on June 6, 2006.

In addition to the above settlement with Bridge Lenders who participated in the legal action, the Company settled its obligation with debenture holders that did not participate ("non-participating debenture holders") in the legal action. These non-participating debenture holders had total debentures of $75,000, plus accrued interest of $9,850, totaling $84,850 as of the settlement date. In conjunction with the above settlement, the Company settled these outstanding non-participating debentures, plus accrued interest, with the issuance of 750,000 shares of common stock valued at $0.0292 per share, or $21,900. The terms of their warrants were not extended, nor are they entitled to receive additional shares based on the Company's common stock achieving a certain average trading price 30 days subsequent to the settlement with the participating debenture holders. During 2004, the Company issued the 750,000 settlement shares.

Management is currently attempting to settle or restructure the remaining debt, and plans to satisfy its existing obligations with the cash derived from the profitable sale of its product.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

Our financial statements are prepared in accordance with accounting principles generally accepted in the United States of America. Preparation of the statements in accordance with these principles requires that we make estimates, using available data and our judgment, for such things as valuing assets, accruing liabilities and estimating expenses. The following is a list of what we believe are the most critical estimations that we make when preparing our financial statements.

Revenue Recognition

Revenue is recognized when products are shipped, title passes and collectibility

is reasonably assured. Allowances for estimated bad debts, sales allowance and discounts are provided when such sales are recorded.

Stock-Based Compensation

Effective January 1, 2006, the Company adopted SFAS 123R which replaces SFAS 123, "Accounting for Stock-Based Compensation" and supersedes Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees." SFAS 123R requires all share-based payments to employees, including grants of employee stock options, to be recognized in the financial statements based on their fair values. Pro forma disclosure is no longer an alternative to financial statement recognition. The adoption of this standard had no effect on operations for the year ended December 31, 2006 as the Company did not issue any options during the period and the Company did not have any vested or unvested options outstanding.

The Black-Scholes option valuation model is used to estimate the fair value of the options granted. The model includes subjective input assumptions that can materially affect the fair value estimates. The model was developed for use in estimating the fair value of traded options or warrants that have no vesting restrictions and that are fully transferable. For example, the expected volatility is estimated based on the most recent historical period of time equal to the weighted average life of the options granted. In management's opinion, this valuation model does not necessarily provide a reliable single measure of the fair value of its employee stock options. During the year ended December 31, 2006 and 2005, the Company did not issue any employee stock options.

Prior to the adoption of SFAS 123R, the Company applied the intrinsic-value-based method of accounting prescribed by APB 25 and related interpretations, to account for its stock options to employees. Under this method, compensation cost was recorded only if the market price of the underlying stock on the date of grant exceeded the exercise price. As permitted by SFAS 123, the Company elected to continue to apply the intrinsic-value-based method of accounting described above, and adopted only the disclosure requirements of SFAS 123. The fair-value-based method used to determine historical pro forma amounts under SFAS 123 was similar in most respects to the method used to determine stock-based compensation expense under SFAS 123R.

In December 2002, the Financial Accounting Standards Board ("FASB") issued SFAS No. 148, "Accounting for Stock-Based Compensation - Transition and Disclosure - an amendment of FASB Statement No. 123." SFAS No. 148 amends SFAS No. 123, "Accounting for Stock-Based Compensation," to provide alternative methods of transition for a voluntary change to the fair value based method of accounting for stock-based employee compensation. In addition, SFAS No. 148 amends the disclosure requirements of SFAS No. 123 to require prominent disclosures in both annual and interim financial statements about the method of accounting for stock-based employee compensation and the effect of the method used on reported results.

We did not grant stock options to employees or directors during the year ended December 31, 2006 and 2005.

We have used stock in the past to raise capital and as a means of compensation to employees.

Derivative Financial Instruments

EITF Issue No. 05-4 "The Effect of a Liquidated Damages Clause on a Freestanding Financial Instrument Subject to EITF Issue No. 00-19, `Accounting for Derivative Financial Instruments Indexed to, and Potentially Settled in, a Company's Own Stock'" ("EITF No. 05-4") addresses financial instruments, such as stock

purchase warrants, which are accounted for under EITF No. 00-19 that may be issued at the same time and in contemplation of a registration rights agreement that includes a liquidated damages clause. The consensus of EITF No. 05-4 has not been finalized.

In November 2005 and October 2006, the Company issued convertible promissory notes and warrants and entered into registration rights agreements (See Note 6). Based on the interpretive guidance in EITF Issue No. 05-4, due to certain factors and the liquidated damage provision in the registration rights agreement, the Company determined that the embedded conversion option and the warrants are derivative liabilities and the registration statement becoming effective in January 2006 and 2007, the value of the registration rights was deemed to be de minimus.

Effects of Recent Accounting Policies

In June 2005, the FASB published Statement of Financial Accounting Standards No. 154, "Accounting Changes and Error Corrections" ("SFAS 154"). SFAS 154 establishes new standards on accounting for changes in accounting principles. Pursuant to the new rules, all such changes must be accounted for by retrospective application to the financial statements of prior periods unless it is impracticable to do so. SFAS 154 completely replaces Accounting Principles

Bulletin No. 20 and SFAS 3, though it carries forward the guidance in those pronouncements with respect to accounting for changes in estimates, changes in the reporting entity, and the correction of errors. The requirements in SFAS 154 are effective for accounting changes made in fiscal years beginning after December 15, 2005. We will apply these requirements to any accounting changes after the implementation date. The adoption of this pronouncement did not have an impact on our financial position, results of operations, or cash flows.

In June 2006, the FASB ratified Emerging Issues Task Force ("EITF") Issue No. 05-1, "Accounting for the Conversion of an Instrument That Becomes Convertible upon the Issuer's Exercise of a Call Option" ("EITF No. 05-1"), which indicates that no gain or loss should be recognized upon the conversion of an instrument that becomes convertible as a result of an issuer's exercise of a call option pursuant to the original terms of the instrument. EITF No. 05-1 is effective for annual or interim periods beginning after June 28, 2006. The adoption of this pronouncement did not have an impact on our financial position, results of operations, or cash flows.

In February 2007, the FASB issued SFAS No. 159, "The Fair Value Option for Financial Assets and Financial Liabilities" ("SFAS 159"). SFAS 159 provides companies with an option to report selected financial assets and liabilities at fair value. The objective of SFAS 159 is to reduce both complexity in accounting for financial instruments and the volatility in earnings caused by measuring related assets and liabilities differently. Generally accepted accounting principles have required different measurement attributes for different assets and liabilities that can create artificial volatility in earnings. The FASB has indicated it believes that SFAS 159 helps to mitigate this type of accounting-induced volatility by enabling companies to report related assets and liabilities at fair value, which would likely reduce the need for companies to comply with detailed rules for hedge accounting. SFAS 159 also establishes presentation and disclosure requirements designed to facilitate comparisons between companies that choose different measurement attributes for similar types of assets and liabilities.

SFAS 159 does not eliminate disclosure requirements included in other accounting standards, including requirements for disclosures about fair value measurements included in SFAS 157 and SFAS No. 107, "Disclosures about Fair Value of Financial Instruments." SFAS 159 is effective for the Company as of the beginning of fiscal year 2009 The adoption of this pronouncement is not expected to have an impact on our financial position, results of operations or cash flows.

In December 2006, the FASB approved FASB Staff Position (FSP) No. EITF 00-19-2, "Accounting for Registration Payment Arrangements" ("FSP EITF 00-19-2"), which specifies that the contingent obligation to make future payments or otherwise transfer consideration under a registration payment arrangement, whether issued as a separate agreement or included as a provision of a financial instrument or other agreement, should be separately recognized and measured in accordance with SFAS No. 5, "Accounting for Contingencies". FSP EITF 00-19-2 also requires additional disclosure regarding the nature of any registration payment arrangements, alternative settlement methods, the maximum potential amount of consideration and the current carrying amount of the liability, if any. The guidance in FSP EITF 00-19-2 amends FASB Statements No. 133, "Accounting for Derivative Instruments and Hedging Activities", and No. 150, "Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity", and FASB Interpretation No. 45, "Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others", to include scope exceptions for registration payment arrangements.

FSP EITF 00-19-2 is effective immediately for registration payment arrangements and the financial instruments subject to those arrangements that are entered into or modified subsequent to the issuance date of this FSP, or for financial statements issued for fiscal years beginning after December 15, 2006, and interim periods within those fiscal years, for registration payment arrangements entered into prior to the issuance date of this FSP. The adoption of this pronouncement is not expected to have an impact on the Company's financial position, results of operations or cash flows.

Effects of Recent Accounting Policies (continued)

In June 2005, the FASB ratified EITF Issue No. 05-2, "The Meaning of `Conventional Convertible Debt Instrument' in EITF Issue No. 00-19, "Accounting for Derivative Financial Instruments Indexed to, and Potentially Settled in, a Company's Own Stock" ("EITF No. 05-2"), which addresses when a convertible debt instrument should be considered "conventional" for the purpose of applying the guidance in EITF No. 00-19. EITF No. 05-2 also retained the exemption under EITF No. 00-19 for conventional convertible debt instruments and indicated that convertible preferred stock having a mandatory redemption date may qualify for the exemption provided under EITF No. 00-19 for conventional convertible debt if the instrument's economic characteristics are more similar to debt than equity. EITF No. 05-2 is effective for new instruments entered into and instruments modified in periods beginning after June 29, 2005. We have applied the requirements of EITF No. 05-2 since the required implementation date. The adoption of this pronouncement did not have an impact on our financial position, results of operations, or cash flows.

In September 2005, the FASB ratified EITF Issue No. 05-7, "Accounting for Modifications to Conversion Options Embedded in Debt Instruments and Related Issues" ("EITF No. 05-7"), which addresses whether a modification to a conversion option that changes its fair value affects the recognition of interest expense for the associated debt instrument after the modification and

whether a borrower should recognize a beneficial conversion feature, not a debt extinguishment, if a debt modification increases the intrinsic value of the debt (for example, the modification reduces the conversion price of the debt). EITF No. 05-7 is effective for the first interim or annual reporting period beginning after December 15, 2005. We adopted EITF No. 05-7 as of the beginning of our interim reporting period that began on January 1, 2006. The adoption of this pronouncement did not have an impact on our financial position, results of operations, or cash flows.

In September 2005, the FASB ratified EITF Issue No. 05-8, "Income Tax Consequences of Issuing Convertible Debt with a Beneficial Conversion Feature" ("EITF No. 05-8"), which addresses the treatment of convertible debt issued with a beneficial conversion feature as a temporary difference under the guidance in SFAS 109. In addition, deferred taxes recognized for a temporary difference of debt with a beneficial conversion feature should be recognized as an adjustment of additional paid-in capital. Entities should apply the guidance in EITF No. 05-8 in the first interim or annual reporting period that begins after December 15, 2005. Its provisions should be applied retrospectively under the guidance in SFAS 154 to all convertible debt instruments with a beneficial conversion feature accounted for under the guidance in EITF No. 00-27 "Application of EITF Issue No. 98-5 "Accounting for Convertible Securities with Beneficial Conversion Features or Contingently Adjustable Conversion Ratios." We have applied the requirements of EITF No. 05-8 to all previously existing convertible debt instruments with a beneficial conversion feature and will apply the requirements of EITF No. 05-8 for all new convertible debt instruments with a beneficial conversion feature. The adoption of this pronouncement for new convertible debt instruments with a beneficial conversion feature did not have an impact on our financial position, results of operations or cash flows.

In February 2006, the FASB published Statement of Financial Accounting Standards No. 155, "Accounting for Certain Hybrid Financial Instruments - an amendment of FASB Statements No. 133 and 140" ("SFAS 155"). SFAS 155 resolves issues addressed in SFAS 133 Implementation Issue No. D1, "Application of Statement 133 to Beneficial Interests in Securitized Financial Assets." The requirements in SFAS 155 are effective for all financial instruments acquired or issued after the beginning of an entity's first fiscal year that begins after September 15, 2006. The adoption of this pronouncement is not expected to have an impact on our financial position, results of operations, or cash flows.

In July 2006, the FASB released Interpretation No. 48, "Accounting for Uncertainty in Income Taxes--an interpretation of FASB Statement No. 109" ("FIN 48"), which clarifies the accounting and reporting for uncertainty in income tax law. FIN 48 prescribes a comprehensive model for the financial statement recognition, measurement, presentation and disclosure of uncertain tax positions taken or expected to be taken in income tax returns. The provisions of FIN 48 are effective after December 15, 2006. Earlier adoption is permitted as of the beginning of an enterprise's fiscal year, provided the enterprise has not yet issued financial statements, including financial statements for any interim period for that fiscal year. The cumulative effects, if any, of applying FIN 48 will be recorded as an adjustment to accumulated deficit as of the beginning of the period of adoption. The adoption of this pronouncement is not expected to have an impact on our financial position, results of operations, or cash flows.

In September 2006, the FASB issued SFAS No. 157, "Fair Value Measurements" ("SFAS 157"). SFAS 157 defines fair value, establishes a framework for measuring fair value in accordance with accounting principles generally accepted in the U.S., and expands disclosures about fair value measurements. SFAS 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007, with earlier application encouraged. Any cumulative effect will be recorded as an adjustment to the opening accumulated deficit balance, or other appropriate component of equity. The adoption of this pronouncement is not expected to have an impact on our financial position, results of operations, or

cash flows.

In September 2006, the SEC staff issued Staff Accounting Bulleting ("SAB") No. 108, Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements ("SAB 108"). SAB 108 was issued in order to reduce the diversity in practice in how public companies quantify misstatements of financial statements, including misstatements that were not material to prior years' financial statements. SAB 108 is effective for fiscal year 2007. The adoption of this pronouncement is not expected to have an impact on our financial position, results of operations, or cash flows.

In October 2005, the FASB issued FSP FAS 123(R)-2, "Practical Accommodation to the Application of Grant Date as Defined in FASB Statement No. 123(R)", which provides clarification of the concept of mutual understanding between employer and employee with respect to the grant date of a share-based payment award. This FSP provides that a mutual understanding of the key terms and conditions of an award shall be presumed to exist on the date the award is approved by management if the recipient does not have the ability to negotiate the key terms and conditions of the award and those key terms and conditions will be communicated to the individual recipient within a relatively short time period after the date of approval. This guidance was applicable upon the initial adoption of SFAS 123(R). The adoption of this pronouncement did not have an impact on our financial position, results of operations, or cash flows.

ITEM 7. FINANCIAL STATEMENTS

The Company's financial statements for the years ended December 31, 2006 and 2005 are included herein and consist of:

Report of Independent Registered Public Accounting Firm	F-1
Balance Sheet	F-2
Statements of Operations	F-3
Statement of Changes in Stockholders' Deficiency	F-4-9
Statements of Cash Flows	F-10
Notes to Financial Statements	F-11

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

During the year ended December 31, 2006, no change in accountants occurred and there were no disagreements with accountants.

ITEM 8A. CONTROLS AND PROCEDURES

Evaluation and Disclosure Controls and Procedures

The Company, under the supervision and with the participation of the Company's management, including the Company's principal executive officer and principal

financial officer, has evaluated the effectiveness of the design and operation of the Company's "disclosure controls and procedures," as such term is defined in Rules 13a-15e promulgated under the Exchange Act as of this report. Based upon that evaluation, the principal executive officer and principal financial officer have concluded that the Company's disclosure controls and procedures were not effective as of the end of the period covered by this report to provide reasonable assurance that information required to be disclosed by the Company in reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in SEC rules and forms.

Our independent registered public accountants have reported to our Board of Directors certain matters involving internal controls that they considered to be reportable conditions and material weaknesses, under standards established by the Public Accounting Oversight Board. The first reportable condition we identified relates to limited segregation of duties.

Management is aware that there is a lack of segregation of duties at the Company due to the small number of employees managing administrative and financial matters. This constitutes a significant deficiency in the financial reporting. Management has mitigated these factors by hiring an independent accountant/bookkeeper to review and compile our financial statements on a quarterly and annual basis.At this time, management has decided that considering the employees involved, the control procedures in place and the potential benefits of adding additional employees to clearly segregate duties does not justify the additional expense.Management will periodically reevaluate this situation. If the situation changes and sufficient capital is secured, it is the Company's intention to increase staffing to mitigate the current lack of segregation of duties within the general administrative and financial functions.

The second reportable condition identified is in our inability to ensure that the accounting for our debt and equity-based transactions is accurate and complete. This condition was considered a material weakness. In recent years we have consummated a series of complex debt and equity transactions involving the application of highly specialized accounting principles. We are evaluating certain corrective measures we may take including the possibility of hiring an outside consultant to provide us with the guidance we need at such times that we may engage in these complex transaction.

Changes in Internal Controls

Management has evaluated the effectiveness of the disclosure controls and procedures as of December 31, 2006. Based on such evaluation, management has concluded that the disclosure controls and procedures were not effective for their intended purpose described above.

Given these reportable conditions and material weaknesses, management devoted additional resources to resolving questions that arose during the period covered by this report. As a result we are confident our financial statements as of December 31, 2006 and 2005 and for the years then ended fairly present in all material respects our financial condition and results of operations.

There were no other changes to the internal controls during the fourth quarter ended December 31, 2006 that have materially affected or that are reasonably likely to affect the internal controls.

Limitations on the Effectiveness of Controls

A control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within a company have been detected. The Company's disclosure controls and procedures are designed to provide reasonable assurance of achieving its objectives. The Company's principal executive officer and principal financial officer concluded that the Company's disclosure controls and procedures are effective at that reasonable assurance level.

ITEM 8B. OTHER INFORMATION

NONE

PART III

ITEM 9. DIRECTORS, EXECUTIVE OFFICERS, PROMOTERS AND CONTROL PERSONS; COMPLIANCE WITH SECTION 16(A) OF THE EXCHANGE ACT

At year-end 2006, the Company's Directors, Executive Officers and Scientific Advisory Board Members were:

Name	Age	Position(s) with the Company
David A. Conway	65	Director, Chairman,President, Chief Executive Officer and Chief Financial Officer
John J. Clarke ++	64	Director
Ronald W. Hart +	64	Chairman, Scientific Advisory Board
Mohamed M. Salem +	55	Scientific Advisory Board
Marshall S. Sterman++	75	Director
Richard Wilson +	81	Scientific Advisory Board
Mostafa K. Tolba +	85	Scientific Advisory Board

+ Members of the Advisory Board will receive an honorarium, in the form of cash or common stock, for their service at the discretion of the Board of Directors.

++ Member of Audit Committee and Compensation Committee. Mr. Sterman, by reason of education, training and experience is the Company's "recognized financial expert" on the Audit Committee. In February 2007, John J. Clarke replaced Mr. Sterman as the Company's "recognized financial expert" on the Audit Committee

David A. Conway

Mr. Conway was elected to the Board of Directors in 1997 and joined the Company as President and Chief Executive Officer in 1998. Previously, he held the positions of President and COO of a privately held public relations and marketing company; Director and VP Administration of KDI Corporation (NYSE); VP Administration Keene Corporation (NYSE) and earlier positions with CBS and Goldman Sachs & Co. Mr. Conway, who served as an infantry officer in the US Army, holds undergraduate and graduate degrees from Fordham University and is listed in Who's Who in America.

John J. Clarke

John J. Clarke rejoined the Company's Board of Directors in March 2004. Mr. Clarke had previously served as a member of the Company's Board of Directors from July 1997 to February 2000 when he resigned from the Board due to his heavy workload. Mr. Clarke is a Principal and co-founder of the Baldwin and Clarke Companies, a diversified financial services organization, where he has been employed since 1976, and is a founding director of two New Hampshire commercial banks. Mr. Clarke currently serves as a Director of Centrix Bank.

Ronald W. Hart (Ph.D.)

Dr. Hart agreed to form the Board of Scientific Advisors in 2000 and became Chairman at that time. Dr. Hart is an internationally recognized scientist and scholar who was Director of the National Center for Toxicological Research and was named "Distinguished Scientist in Residence" by the US Food and Drug Administration in 1992. Recognized for his pioneering work on aging and his studies on nutrition and health, Dr. Hart has been appointed visiting professor at a number of universities, including Cairo University, Seoul National University and Gangzhou University. He received his doctorate in physiology and biophysics from the University of Illinois.

Mohamed M. Salem (MD/PhD.)

Dr. Salem was appointed to the Scientific Advisory Board in early 2001. Dr. Salem is Professor of Occupational and Environmental Medicine at the Kasr El-Aini School of Cairo University. An internationally recognized expert on the health effects of environmental and water contaminants including pesticides, lead and other metals, Dr. Salem is credited with establishing infectious disease control programs at medical centers and other public entities throughout the Middle East. Dr. Salem is a principal of Salem Industries, an import and export company, which is one of the leading suppliers of chemicals and oil field equipment in the Middle East. Dr. Salem holds both an M.D. and Ph.D. from Cairo University.

Marshall S. Sterman

Mr. Sterman was elected to the Board of Directors in 2000. Mr. Sterman is President of the Mayflower Group, a Massachusetts based merchant bank, where he has been employed since 1986. He previously served as managing partner of Cheverie and Company and MS Sterman & Associates, merchant banking firms and principal of Sterman & Gowell Securities, an investment banking and securities firm. Mr. Sterman served as an officer in the US Navy and holds his BA from Brandeis University and his MBA from Harvard University.

Richard Wilson (Ph.D.)

Dr. Wilson was appointed to the Scientific Advisory Board in February 2001. Dr. Wilson is the Mallinckrodt Research Professor of Physics at Harvard University. Dr. Wilson is one of the foremost scientific authorities in the fields of water quality remediation and purification, and is currently Professor of the Energy Research Group at the University of California. Dr. Wilson is a member of the Advisory Board of the Atlantic Legal Foundation, and is one of the principal scientists studying the resolution of the water problems in Chernobyl and in Bangladesh where toxic levels of arsenic contaminate the water supply. Dr. Wilson holds his Ph.D. from Oxford University.

Mostafa K. Tolba (Ph.D.)

Dr. Tolba joined the Scientific Advisory Board in June 2001. Dr. Tolba served as Under-Secretary-General of the United Nations, and Executive Director of the United Nations Environmental Program from 1976 to 1992. Dr. Tolba is currently President of the International Center for Environment and Development headquartered in Geneva, Switzerland, and Emeritus Professor of Science at the Kasr El-Aini School of Medicine at Cairo University. He received his Ph.D. in Macrobiology from Imperial College, London, England.

Marshall S. Sterman and John J. Clarke are the members of the Company's Audit Committee. The Board of Directors has determined that Mr. Sterman is an "audit committee financial expert" as defined in Item 401(e) of Regulation S-B.

On January 15, 2007, Leslie J. Kessler was appointed President of WaterChef, Inc. On February 1, 2007, Ms. Kessler was appointed Chief Executive Officer and was elected to the Board of Directors.

On January 19, 2007, Dr. Ronald W. Hart, Chairman of the Company's Board of Scientific Advisors, was appointed to the Board of Directors of WaterChef, Inc.

On January 29, 2007, Mr. Conway resigned as President and Chief Executive Officer of the Corporation, and as a member of the Board of Directors. On February 12, 2007, Marshall Sterman resigned as a member of the Board of Directors.

Effective with Mr. Conway's resignation, Mr. Clarke became Chairman of the Board, and upon Mr. Sterman's resignation he became Chairman of the Audit and Compensation Committees of the Board.

Compliance with Section 16(a) of the Securities Exchange Act of 1934

Section 16(a) of the Securities Exchange Act of 1934, as amended, requires our executive officers and directors, and persons who beneficially own more than ten percent of our common stock, to file initial reports of ownership and reports of changes in ownership with the Securities and Exchange Commission. Executive officers, directors and greater than ten percent beneficial owners are required by Securities and Exchange Commission regulations to furnish us with copies of all Section 16(a) forms they file. Based upon a review of the copies of such forms furnished to us and written representations from our executive officers and directors, we believe that during the year ended December 31, 2006 there were no delinquent filers except as follows: Marshall S. Sterman filed a Form 5/A on February 8, 2007 in which he reported transactions that occurred on May 15, 2006, May 24, 2006, June 6, 2006, and June 12, 2006 that were not timely reported on a Form 4 (four transactions) and John J. Clarke filed a Form 5 on February 8, 2007 for transactions that occurred on May 24, 2006,and June 6, 2006 that were not timely reported on a Form 4 (two transactions).

Code of Ethics

We adopted a code of ethics in 2005 that was filed as Exhibit 14.1 to our Quarterly Report on Form 10-QSB filed with the Securities and Exchange Commission on August 15, 2005. The code of ethics applies to each of our directors and officers, including the chief financial officer and chief executive officer, and all of our other employees and the employees of our subsidiaries.

ITEM 10. EXECUTIVE COMPENSATION

SUMMARY COMPENSATION TABLE

Name and Principal Position	Year	Salary ($)	Bonus ($)	All Other Annual Compensation ($)	Total ($)
David A. Conway President/CEO	2006	$350,000	--	--	$350,000

EMPLOYMENT AGREEMENTS

Mr. Conway entered into a five-year employment agreement in January 2004. The agreement provides for base salary of $350,000 per year, participation in the Company's employee benefit programs and a life insurance policy in the amount of $5,000,000 which was never purchased. In addition, Mr. Conway was granted a stock appreciation right, vesting at 20% per year for five years, for 5,000,000 shares of Water Chef common stock at a strike price of $0.25 per share. Mr. Conway was originally granted stock options in January 2004 that were later converted to stock appreciation rights. Under the terms of the Employment Agreement if the employee is terminated by the Company for other than cause, the Employee is entitled to receive an amount equal to his monthly base pay multiplied by 24 months. In the event of a Change of Control the Company is required to pay to the Employee an amount equal to his monthly base salary multiplied by thirty-six. Upon his resignation as President and Chief Executive Officer, Mr. Conway relinquished his right to unpaid, accrued salary and to the unexercised stock appreciation rights.

The Company did not issue any stock options or common stock appreciation rights during fiscal 2006.

The Company has no long-term incentive plans at this time.

Outstanding Equity Awards at Fiscal Year-End

Name	Number of Securities Underlying Unexercised Options (#) exercisable	Number of Securities Underlying Unexercised Options (#) exercisable	Equity Incentive Plan Awards; Number of Securities Underlying Unexercised Unearned Options	Opt
David A. Conway	3,600,000	1,400,000	0	

DIRECTORS' COMPENSATION

Name	Fees Earned or Paid in Cash	Stock Awards	Option Awards
John J. Clarke	$25,000	$ --	120,600
Marshall S. Sterman	25,000	--	120,600

Directors of the Company do not receive cash compensation for serving as members; they are reimbursed for their out of pocket expenses related to meetings and other Company related activity for which they are called upon. In the past certain directors have received common stock for service to the Company.

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In 2006, Mr. Sterman was compensated at the rate of $6,000 per month for consulting services performed for the Company. The Company may pay for these services in cash or stock. The Company terminated this agreement in June 2006. There is $317,500 due to him for this service as of December 31, 2006. On February 12, 2007, Mr. Sterman resigned from the Board of Directors and waived his rights to any accrued compensation owed to him by the Company.

The Company's directors have been paid success fees for helping the Company in various equity and debt financings in previous years. These payments have been both in cash and common stock, such payments being made based on industry-wide standards and arms-length transactions.

ITEM 11. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS

Set forth below is information as of December 31, 2006, concerning stock ownership of all persons known by the Company to own beneficially 5% or more of the any class of the securities of the Company, all Directors, the Executive Officers, and all Directors and Executive Officers of the Company as a group based on the number of shares of common stock issued and outstanding as of the date of this report. For purposes of the report, beneficial ownership is defined in accordance with the Rules of the Securities and Exchange Commission and generally means the power to vote and/or dispose of the securities regardless of any economic interest.

	Common Stock Beneficially Owned(1)		Series A Preferred Stock Beneficially Owned(1)		Series D Prefer Stock Beneficia Owned(1)	
	Shares	%	Shares	%	Shares	
David A. Conway (2) (3) Water Chef, Inc. 1007 Glen Cove Ave., Suite 1	25,110,782	12.6%	--	--	--	

Glen Head, NY 11545						
Marshall S. Sterman 46 Neptune Street Beverly, MA 01915	2,100,000(5)	1.1%	--	--	--	
John J. Clarke 116B S. River Rd. Bedford, NH 03110	2,631,700(6)	1.4%	--	--	--	
Goldman, Sachs & Co. (4) 85 Broad Street New York, NY 10004	16,773,651	8.4%	--	--	--	
Jerome Asher & Anne Asher JTWROS 2701 N Ocean Blvd Apt E-202 Boca Raton, FL 33431	--	--	5,000	9.5%	--	
Robert D. Asher 72 Old Farm Road Concord, MA 01742	--	--	5,000	9.5%	--	
John A. Borger 806 E Avenida Pico Suite I PMB #262 San Clemente, CA 92673	--	--	--	--	10,000	1
C Trade Inc 25-40 Shore Blvd., Ste. 6C Astoria, NY 11102	--	--	--	--	--	
Robert Kaszovitz 1621 51st Street Brooklyn, NY 11204	--	--	--	--	--	
Kollel Metzioynim Lhoroah 254 Wallabout St., Apt. 2 Brooklyn, NY 11206	--	--	--	--	--	
Olshan Grundman Frome Rosenzweig & Wolosky LLP 65 East 55th Street New York, NY 10022	--	--	--	--	--	
Shirley M. Wan 5455 Chelsen Wood Dr. Lawrence, NY 11559	--	--	--	--	--	
All executive officers and directors as a Group (2)	27,742,482	15.0%	--	--	--	

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1. Total Voting Shares are comprised of all common shares issued and outstanding.

2. Includes 6,310,464 shares held in an IRA Trust.

3. Effective with his resignation as President and Chief Executive Officer on January 29, 2007 Mr. Conway has returned to the Company 20,000,000 shares of common stock owned by him and his affiliates.

4. According to a Schedule 13G/a filed by Goldman, Sachs & Co. filed on February 12, 2007, it and The Goldman Sachs Group, Inc. have sole dispositive power and sole voting power with respect to the 16,773,651 shares.

5. Includes 850,000 shares of common stock owned directly by Marshall Sterman and warrants to purchase 1,250,000 shares of common stock.

6. Includes 1,381,700 shares of common stock owned directly by John J. Clarke and warrants to purchase 1,250,000 shares of common stock.

ITEM 12. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS

Beginning on January 1, 2002, Mr. Sterman was compensated at the rate of $6,000 per month for consulting services performed for the Company. In 2004 Mr. Sterman's monthly compensation increased to $10,000. The Company may pay for these services in cash or stock . Mr. Sterman's consulting agreement was terminated in June 2006. Mr. Sterman resigned from the Board of Directors on February 12, 2007 and waived his right to any accrued compensation and director fees owed to him by the Company.

ITEM 13. EXHIBITS

(a) Exhibits:

Number	Description of Exhibit
3.1	Amended and Restated By-Laws of Water Chef, Inc. - Incorporated herein by reference to Exhibit 3(ii) to the Form 10-KSB/A filed November 17, 2003.
3.2	Amended and Restated Certificate of Incorporation of Water Chef, Inc. - Incorporated herein by reference to Exhibit 3.2 to the Form SB-2 filed January 24, 2005.
3.3	Certificate of Amendment of Restated Certificate of Incorporation of Water Chef, Inc. dated August 2, 1993 - Incorporated herein by reference to Exhibit 3.3 to the Form SB-2 filed January 24, 2005.
3.4	Certificate of Amendment of Restated Certificate of Incorporation of Water Chef, Inc. dated August 2, 1992 - Incorporated herein by reference to Exhibit 3.4 to the Form SB-2 filed January 24, 2005.
3.5	Certificate for Renewal and Revival of Certificate of Incorporation - Incorporated herein by reference to Exhibit 3.5 to the Form SB-2 filed January 24, 2005.
3.6	Certificate of Amendment of Restated Certificate of Incorporation of Water Chef, Inc. dated February 20, 2002 - Incorporated herein by reference to Exhibit 3.6 to the Form SB-2 filed January 24, 2005.
3.7	Certificate of Correction filed to correct a certain error

Number	Description of Exhibit
	in the Certificate of Amendment of the Restated Certificate of Incorporation of Water Chef, Inc. dated May 7, 2004 - Incorporated herein by reference to Exhibit 3.7 to the Form SB-2 filed January 24, 2005.
4.1	Certificate of Designation of Series A Preferred Stock of Water Chef, Inc. - Incorporated herein by reference to Exhibit 4.1 to the Form 10-KSB/A filed November 17, 2003.
4.2	Certificate of Designation of Series C convertible preferred stock of Water Chef, Inc. - Incorporated herein by reference to Exhibit 4.2 to the Form 10-KSB/A filed November 17, 2003.
4.3	Certificate of Designation of Series D Preferred Stock of Water Chef, Inc. - Incorporated herein by reference to Exhibit 4.3 to the Form 10-KSB/A filed November 17, 2003.
4.4	Certificate of Designation of Series F convertible preferred stock of Water Chef, Inc. - Incorporated herein by reference to Exhibit 4.4 to the Form SB-2 filed January 24, 2005.

Number	Description of Exhibit
4.5	Series B Warrant to Purchase Common Stock and Allonge to and Amendment and Extension of Common Stock Purchase Warrant - Incorporated herein by reference to Exhibit 4.4 to the Form 10-KSB/A filed November 17, 2003.
4.6	Series B Second Allonge to and Amendment and Extension of Common Stock Purchase Warrant - Incorporated herein by reference to Exhibit 4.6 to the Form SB-2 filed January 24, 2005.
4.7	Subordinated Debentures - Incorporated herein by reference to Exhibit 4.5 to the Form 10-KSB/A filed November 17, 2003.
10.1	Loan Agreement, dated as of November 16, 2005, by and between Water Chef, Inc. and Southridge Partners LP - Incorporated herein by reference to Exhibit 99.1 to the Form 8-K filed November 23, 2005.
10.2	Registration Rights Agreement, dated as of November 16, 2005, by and between Water Chef, Inc. and Southridge Partners LP - Incorporated herein by reference to Exhibit 99.2 to the Form 8-K filed November 23, 2005.
10.3	Promissory Note issued by Water Chef, Inc. on November 16, 2005 to Southridge Partners LP for the principal sum of $250,000 - Incorporated herein by reference to Exhibit 99.3 to the Form 8-K filed November 23, 2005.
10.4	Three Year Warrant issued to Southridge Partners LP, dated November 16, 2005, to purchase 430,000 shares of common stock at a price of $0.14 per share - Incorporated herein by reference to Exhibit 9.4 to the Form 8-K filed November 23, 2005.

10.5	Loan Agreement, dated as of October 11, 2006, by and between Water Chef, Inc. and Southridge Partners LP - Incorporated herein by reference to Exhibit 9.4 to the Form 8-K filed October 19, 2006.
10.6	Registration Rights Agreement, dated as of October 11, 2006, by and between Water Chef, Inc. and Southridge Partners LP - Incorporated herein by reference to Exhibit 9.4 to the Form 8-K filed October 19, 2006.
10.7	Promissory Note issued by Water Chef, Inc. on October 11, 2006 to Southridge Partners LP for the principal sum of $300,00 - Incorporated herein by reference to Exhibit 9.4 to the Form 8-K filed October 19, 2006.
10.8	Three Year Warrant issued to Southridge Partners LP, dated October 11, 2006, to purchase 882,352 shares of common stock at a price of $0.085 per share - Incorporated herein by reference to Exhibit 9.4 to the Form 8-K filed October 19, 2006.
31.1*	Certification of Chief Executive Officer and Chief Financial officer pursuant to Section 302 of the Sarbanes-Oxley Act.
32.2*	Certification of Chief Executive Officer and Chief Financial Officer pursuant to 8 U.S.C. Section 1350 As adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. * filed herewith

ITEM 14. PRINCIPAL ACCOUNTANT FEES

Our principal accountant for the audit of our annual financial statements for our fiscal years ended December 31, 2005 and 2004 was Marcum & Kliegman LLP ("M&K").

The following table shows the fees paid or accrued by us during the periods indicated.

	Year ended	
Type of Service	2006	2005
Audit fees (1)	$125,000	$105,000
Audit-Related Fees (2)	--	--
Tax Fees (3)	--	--
All Other Fees (4)	--	--
Total	$125,000	$105,000

(1) Comprised of the audit of our annual financial statements and reviews of our quarterly financial statements.

(2) Comprised of assurance services in connection with employee benefit plan audits, due diligence related to mergers and acquisitions, accounting

consultations related to mergers and acquisitions, internal control reviews, attest services that are not required by statute or regulation and consultation concerning financial accounting and reporting standards.

(3) Comprised of services for tax compliance, tax return preparation, tax advice and tax planning.

(4) Fees related to other filings with the SEC.

Under the Sarbanes-Oxley Act of 2002, all audit and non-audit services performed by the Company's independent accountants must now be approved in advance by the Audit Committee to assure that such services do not impair the accountants' independence from the Company. Accordingly, the Audit Committee has adopted an Audit and Non-Audit Services Pre-Approval Policy (the "Policy") which sets forth the procedures and the conditions pursuant to which services to be performed by the independent accountants are to be pre-approved. Pursuant to the Policy, certain services described in detail in the Policy may be pre-approved on an annual basis together with pre-approved maximum fee levels for such services. The services eligible for annual pre-approval consist of services that would be included under the categories of Audit Fees, Audit-Related Fees, Tax Fees and All Other Fees in the above table as well as services for limited review of actuarial reports and calculations. If not pre-approved on an annual basis, proposed services must otherwise be separately approved prior to being performed by the independent accountants. In addition, any services that receive annual pre-approval but exceed the pre-approved maximum fee level also will require separate approval by the Audit Committee prior to being performed. The Audit Committee may delegate authority to pre-approve audit and non-audit services to any member of the Audit Committee, but may not delegate such authority to management.

All of the engagements and fees for the year ended December 31, 2006 were approved by the Audit Committee. Of the total number of hours expended during M&K's engagement to audit the Company's financial statements for the year ended December 31, 2006, none of the hours were attributed to work performed by persons other than M&K's full-time, permanent employees.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this Report to be signed on its behalf by the undersigned thereunto duly authorized.

WATERCHEF, INC.

March 30, 2007 /s/ Leslie J. Kessler

Date

Leslie J. Kessler
President, Chief Executive Officer and Chief Financial Officer (Principal Operating Officer)

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Stockholders of Water Chef, Inc.
Glen Head, New York

We have audited the accompanying balance sheet of Water Chef, Inc., (a development stage company) as of December 31, 2006 and the related statements of operations, stockholders' deficiency and cash flows for the years ended December 31, 2006 and 2005 and for the period from January 1, 2002 (commencement as a development stage company) to December 31, 2006. 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. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining on a test basis, evidence supporting the amounts and disclosures in the financial statements, 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 Water Chef, Inc., (a development stage company) as of December 31, 2006 and the results of its operations and its cash flows for the years ended December 31, 2006 and 2005 and for the period from January 1, 2002 (commencement as a development stage company) to December 31, 2006 in conformity with accounting principles generally accepted in the United States of America.

The accompanying financial statements have been prepared assuming the Company will continue as a going concern. As discussed in Note 2 to the financial statements, the Company has had recurring losses, and has a working capital and stockholders' deficiency as of December 31, 2006. These conditions raise substantial doubt about its ability to continue as a going concern. Management's plans in regard to these matters are also described in Note 2. The financial statements do not include any adjustments that might result from the outcome of this uncertainty.

/s/ Marcum & Kliegman LLP

Marcum & Kliegman LLP

New York, New York
March 19, 2007

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WATER CHEF, INC.
(A Development Stage Company Commencing January 1, 2002)
BALANCE SHEET
DECEMBER 31, 2006

ASSETS

Current Assets:	
Cash	$ 99,716
Prepaid expenses	19,282
Total Current Assets	118,998
Patents and trademarks, Net	15,403
Deferred financing costs	4,687
Other assets	3,162
TOTAL ASSETS	$ 142,250

LIABILITIES AND STOCKHOLDERS' DEFICIENCY

Current Liabilities:	
Accounts payable and accrued expenses	$ 385,975
Accrued compensation	561,583
Accrued consulting and director fees	468,333
Notes payable (including accrued interest of $343,265)	990,856
Convertible promissory note including accrued interest of $5,000 and net of debt discount of $69,800)	235,200
Fair-value of detachable warrants and options	293,000
Fair-value of embedded conversion option	117,400
Accrued dividends payable	189,871
Total Current Liabilities	3,242,218
Long-Term Liabilities:	
Loans payable to stockholder (including accrued interest of $152,957)	525,738
TOTAL LIABILITIES	3,767,956
COMMITMENTS AND CONTINGENCIES	
STOCKHOLDERS' DEFICIENCY:	
Preferred stock, $.001 par value; 10,000,000 shares authorized; 188,917 shares issued and outstanding,	

(liquidation preference $2,267,350)	189
Common stock, $.001 par value;	
340,000,000 shares authorized;	
198,977,497 shares issued;	
198,973,097 shares outstanding	198,977
Additional paid-in capital	22,836,764
Treasury stock, 4,400 common shares, at cost	(5,768)
Accumulated deficit through December 31, 2001	(14,531,596)
Deficit accumulated during development stage	(12,124,272)
TOTAL STOCKHOLDERS' DEFICIENCY	(3,625,706)
TOTAL LIABILITIES AND STOCKHOLDERS' DEFICIENCY	$ 142,250

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

WATER CHEF, INC.

(A Development Stage Company Commencing January 1, 2002)

STATEMENTS OF OPERATIONS

	Years Ended December 31, 2006	2005	For t period from 2002 (Da Commencem a Develo Stage Co to Decem 200
Sales	$ 115,000	$ 260,000	$ 4
Costs and Expenses (Income):			
Cost of sales	114,000	42,000	5
Selling, general and administrative - including stock based compensation of $767,699 and $53,827 for the year ended December 31, 2006 and 2005, respectively and $1,545,089 for the period from January 1, 2002 to December 31, 2006	1,559,464	1,194,577	5,6
Non-dilution agreement termination costs	--	--	2,4
Interest expense (including interest expense for related party of $23,868 in both 2006 and 2005 and $119,340 for the period January 1, 2002 to December 31, 2006)	380,553	244,191	1,1
Financing costs - extension of warrants	--	74,700	
Loss on settlement of debt	--	--	2,6
Stock appreciation rights	--	(121,340)	
Change in fair value of warrants and			

embedded conversion option	133,900	(5,800)	1
	2,187,917	1,428,328	12,5
Net loss	(2,072,917)	(1,168,328)	(12,1
Deemed dividend on preferred stock	--	--	(2,0
Preferred stock dividends	(42,401)	(66,436)	(5
Net loss applicable to common stockholders	$ (2,115,318)	$ (1,234,764)	$ (14,7
Basic and Diluted Loss Per Common Share	$ (0.01)	$ (0.01)	
Weighted Average Common Shares Outstanding - Basic and Diluted	193,408,939	166,132,433	

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

WATER CHEF, INC.
STATEMENT OF STOCKHOLDERS' DEFICIENCY
For the Period from January 1, 2002 (Date of Commencement as a
Development Stage Company) to December 31, 2006

	Preferred Stock		C
	Shares	Amount	Shares
BALANCE - JANUARY 1, 2002	145,500	$ 146	86,614,
Extension of life of warrants	--	--	-
Proceeds from sale preferred stock ($1.00 per share)	125,000	125	-
Proceeds from sale of common stock ($0.025 per share)	--	--	2,500,
Common stock issued for services ($0.08 per share)	--	--	450,
Collection of subscription receivable	--	--	-
Net Loss	--	--	-
BALANCE - DECEMBER 31, 2002	270,500	$ 271	89,564,
Proceeds from sale of preferred stock March 31, 2003 ($1.00-$2.00 per share)	62,500	63	-
June 30, 2003			

($0.50 per share)	75,000	75	-
September 30, 2003			
($1.00-$2.40 per share)	163,281	163	-
December 31, 2003			
($1.33-$2.80 per share)	145,450	145	-
Preferred stock issued for services			
March 31, 2003			
($1.00 per share)	30,000	30	-
June 30, 2003			
($1.00 per share)	51,250	51	-
September 30, 2003			
($1.00 per share)	67,035	67	-
December 31, 2003			
($1.88-$4.00 per share)	22,150	22	-
Collection of subscription receivable	--	--	-
Write-off of subscription receivable	--	--	-
Net Loss	--	--	-
BALANCE - DECEMBER 31, 2003	887,166	$ 887	89,564,
Proceeds from sale of preferred stock			
March 31, 2004			
($2.40-$4.80 per share)	130,077	130	-
June 30, 2004			
($0.80 per share)	15,625	16	-
Preferred stock issued for services			
March 31, 2004			
($2.00-$4.80 per share)	49,433	49	-
Proceeds from sale of common stock			
September 30,2004			
($0.03-$0.15 per share)	--	--	2,541,
December 31, 2004			
($0.05-$0.10 per share)	--	--	2,487,
Common stock issued for services			
March 31, 2004			
($0.05 Per share)	--	--	477,
September 30,2004			
($0.05-$0.15 per share)	--	--	1,857,
December 31, 2004			
($0.08-$0.10 per share)	--	--	532,
Preferred stock dividend	--	--	-
Common stock issued for satisfaction of liabilities			
June 30, 2004			
($0.15 per share)	--	--	37,786,
December 31, 2004			
($0.134 per share)	--	--	411,

The accompanying notes are an integral part of these financial state

WATER CHEF, INC.

STATEMENT OF STOCKHOLDERS' DEFICIENCY
For the Period from January 1, 2002 (Date of Commencement as a
Development Stage Company) to December 31, 2006

	Preferred Stock		C
	Shares	Amount	Shares
Preferred stock converted to common stock			
June 30, 2004	(133,250)	(133)	5,108,
September 30, 2004	(269,263)	(269)	12,103,
December 31, 2004	(65,375)	(65)	3,015,
Net loss	--	--	--
BALANCE - DECEMBER 31, 2004	614,413	$ 615	155,885,
Proceeds from sale of common stock			
March 31,2005			
($0.05 per share)	--	--	200,
June 30,2005			
($0.05-$0.06 per share)	--	--	700,
September 30,2005			
($0.07-$0.10 per share)	--	--	2,455,
December 31, 2005			
($0.05-$0.07 per share)	--	--	3,879,
Common stock issued for services			
March 31, 2005			
($0.05-$0.10 per share)	--	--	230,
December 31, 2005			
($0.05-$0.06 per share)	--	--	407,
Preferred stock dividend	--	--	-
Extension of 1,666,667 warrants	--	--	-
Common stock issued for satisfaction of liabilities			
September 30, 2005			
($0.07 per share)	--	--	571,
December 31, 2005			
($0.142 per share)	--	--	100,
Preferred stock converted to common stock			
March 31, 2005	(55,970)	(56)	2,518,
June 30, 2005	(34,020)	(34)	1,360,
September 30, 2005	(286,650)	(287)	13,382,
December 31, 2005	(2,188)	(2)	87,
Net loss	--	--	-
BALANCE - DECEMBER 31, 2005	235,585	$ 236	181,779,
Proceeds from sale of common stock			
March 21, 2006			
($0.07 per share)	--	--	3,600,
May 8, 2002			
($0.08-$0.10 per share)	--	--	3,769,
June 28, 2006			
($0.10 per share)	--	--	100,
August 17, 2006			
($0.07 per share)	--	--	400,

Common stock issued for services			
March 21, 2006			
($0.06 per share)	--	--	250,
May 8, 2006			
($0.05 per share)	--	--	450,
June 6, 2006			
($0.15 per share)	--	--	166,
Common stock issued for repayment of debt			
February 13, 2006			
($0.11 per share)	--	--	438,
April 3, 2006			
($0.08 per share)	--	--	614,
April 6, 2006			
($0.08 Per share)	--	--	1,959,
June 6, 2006			
($0.10-$0.15 per share)	--	--	3,583,
Preferred stock converted to common stock	(46,668)	(47)	1,866,

The accompanying notes are an integral part of these financial state

WATER CHEF, INC.
STATEMENT OF STOCKHOLDERS' DEFICIENCY
For the Period from January 1, 2002 (Date of Commencement as a
Development Stage Company) to December 31, 2006

	Preferred Stock		C
	Shares	Amount	Shares
Reclassification of derivative liabilities upon conversion of debt	--	--	--
4,000,000 Warrants granted for services, May 18, 2006	--	--	--
2,500,000 Warrants granted for services, May 24, 2006	--	--	--
Reclassification of warrants and embedded conversion option upon issuance of convertible debt	--	--	--
Preferred stock dividend	--	--	--
Net loss	--	--	--
BALANCE - DECEMBER 31, 2006	188,917	$ 189	198,977,

The accompanying notes are an integral part of these financial state
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WATER CHEF, INC.
STATEMENT OF STOCKHOLDERS' DEFICIENCY
For the Period from January 1, 2002 (Date of Commencement as a
Development Stage Company) to December 31, 2006

-continued-	Stock Subscription Receivable	Treasury Stock	Accumulated Deficit Through December 31, 2001
BALANCE - JANUARY 1, 2002	$ (67,500)	$ (5,768)	$(14,531,59
Extension of life of warrants	--	--	--
Proceeds from sale preferred stock ($1.00 per share)	--	--	--
Proceeds from sale of common stock ($0.025 per share)	--	--	--
Common stock issued for services ($0.08 per share)	--	--	--
Collection of subscription receivable	30,200	--	--
Net Loss	--	--	--
BALANCE - DECEMBER 31, 2002	(37,300)	(5,768)	(14,531,59
Proceeds from sale of preferred stock			
March 31, 2003 ($1.00-$2.00 per share)	--	--	--
June 30, 2003 ($0.50 per share)	--	--	--
September 30, 2003 ($1.00-$2.40 per share)	--	--	--
December 31, 2003 ($1.33-$2.80 per share)	--	--	--
Preferred stock issued for services			
March 31, 2003 ($1.00 per share)	--	--	--
June 30, 2003 ($1.00 per share)	--	--	--
September 30, 2003 ($1.00 per share)	--	--	--
December 31, 2003 ($1.88-$4.00 per share)	--	--	--
Collection of subscription receivable	15,500	--	--
Write-off of subscription receivable	21,800	--	--

Net Loss	--	--	--
BALANCE - DECEMBER 31, 2003	--	(5,768)	(14,531,59
Proceeds from sale of preferred stock			
March 31, 2004			
($2.40-$4.80 per share)	--	--	--
June 30, 2004			
($0.80 per share)	--	--	--
Preferred stock issued for services			
March 31, 2004			
($2.00-$4.80 per share)	--	--	--
Proceeds from sale of common stock			
September 30,2004			
($0.03-$0.15 per share)	--	--	--
December 31, 2004			
($0.05-$0.10 per share)	--	--	--
Common stock issued for services			
March 31, 2004			
($0.05 per share)	--	--	--
September 30,2004			
($0.05-$0.15 per share)	--	--	--
December 31, 2004			
($0.08-$0.10 per share)	--	--	--
Preferred stock dividend	--	--	--
Common stock issued for satisfaction of liabilities			
June 30, 2004			
($0.15 per share)	--	--	--
December 31, 2004			
($0.134 per share)	--	--	--

The accompanying notes are an integral part of these financial state

WATER CHEF, INC.
STATEMENT OF STOCKHOLDERS' DEFICIENCY
For the Period from January 1, 2002 (Date of Commencement as a
Development Stage Company) to December 31, 2006

-continued-	Stock Subscription Receivable	Treasury Stock	Accumulated Deficit Through December 31, 2001
Preferred stock converted to common stock			
June 30, 2004	--	--	--
September 30, 2004	--	--	--
December 31, 2004	--	--	--
Net loss	--	--	--
BALANCE - DECEMBER 31, 2004	--	$ (5,768)	$(14,531,59
Proceeds from sale of common stock			

March 31,2005			
($0.05 per share)	--	--	--
June 30,2005			
($0.05-$0.06 per share)	--	--	--
September 30,2005			
($0.07-$0.10 per share)	--	--	--
December 31, 2005			
($0.05-$0.07 per share)	--	--	--
Common stock issued for services			
March 31, 2005			
($0.05-$0.10 per share)	--	--	--
December 31, 2005			
($0.05-$0.06 per share)	--	--	--
Preferred stock dividend	--	--	--
Extension of 1,666,667 warrants	--	--	--
Common stock issued for satisfaction of liabilities			
September 30, 2005			
($0.07 per share)	--	--	--
December 31, 2005			
($0.142 per share)	--	--	--
Preferred stock converted to common stock			
March 31, 2005	--	--	--
June 30, 2005	--	--	--
September 30, 2005	--	--	--
December 31, 2005	--	--	--
Net loss	--	--	--
BALANCE - DECEMBER 31, 2005	--	$ (5,768)	$(14,531,59
Proceeds from sale of common stock			
March 21, 2006			
($0.07 per share)	--	--	--
May 8, 2006			
($0.08-$0.10 per share)	--	--	--
June 28, 2006			
($0.10 per share)	--	--	--
August 17, 2006			
($0.07 per share)	--	--	--
Common stock issued for services			
March 21, 2006			
($0.06 per share)	--	--	--
May 8, 2006			
($0.05 per share)	--	--	--
June 6, 2006			
($0.15 per share)	--	--	--
Common stock issued for repayment of debt			
February 13, 2006			
($0.11 per share)	--	--	--
April 3, 2006			
($0.08 per share)	--	--	--
April 6, 2006			
($0.08 per share)	--	--	--
June 6, 2006			
($0.10-$0.15 per share)	--	--	--

Preferred stock converted to common stock	--	--	--

The accompanying notes are an integral part of these financial state

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WATER CHEF, INC.
STATEMENT OF STOCKHOLDERS' DEFICIENCY
For the Period from January 1, 2002 (Date of Commencement as a
Development Stage Company) to December 31, 2006

-continued-	Stock Subscription Receivable	Treasury Stock	Accumulated Deficit Through December 31, 2001
Reclassification of derivative liabilities upon Conversion of debt	--	--	--
4,000,000 Warrants granted for services, May 18, 2006	--	--	--
2,500,000 Warrants granted for services, May 24, 2006	--	--	--
Reclassification of warrants and the convertible preferred stock embedded conversion option upon issuance of convertible debt	--	--	-
Preferred stock dividend	--	--	--
Net loss	--	--	--
BALANCE - DECEMBER 31, 2006	$ --	$ (5,768)	$(14,531,5

The accompanying notes are an integral part of these financial state

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WATER CHEF, INC.

(A Development Stage Company Commencing January 1, 2002)

STATEMENTS OF CASH FLOWS

	Year Ended December 31, 2006	2005
CASH FLOWS FROM OPERATING ACTIVITIES		
Net loss	$(2,072,917)	$(1,168,3
Adjustments to reconcile net loss to net cash used in operating activities		
Amortization of patents	1,854	1,8
Interest expense - deferred financing	7,500	2,8
Stock based compensation	767,699	53,8
Accretion of debt discount	217,320	75,2
Change in fair value of warrants and embedded conversion option	133,900	(5,8
Loss on settlement of debt	--	--
Non-dilution agreement termination cost	--	--
Inventory reserve	--	--
Write-off of stock subscription receivable	--	--
Financing costs - warrant extension	--	74,7
Change in assets and liabilities		
Inventory	30,000	(30,0
Prepaid expenses	3,682	(5,8
Accounts payable, accrued expenses, accrued dividends, accrued compensation, accrued consulting and director fees, customer deposits and other current liabilities	(74,148)	422,3
NET CASH USED IN OPERATING ACTIVITIES	(985,110)	(579,2
CASH FLOWS FROM FINANCING ACTIVITIES		
Reduction of stock subscription receivable	--	20,0
Proceeds from sale of preferred stock	--	--
Proceeds from sale of common stock	568,000	494,9
Proceeds from sale of common stock to be issued	--	--
Deferred financing costs	(7,500)	(7,5
Proceeds from convertible promissory note	300,000	250,0
Repayment of notes payable	(20,269)	(15,3
NET CASH PROVIDED BY FINANCING ACTIVITIES	840,231	742,0
NET (DECREASE) INCREASE IN CASH	(144,879)	162,8
CASH AT BEGINNING OF YEAR	244,595	81,7
CASH AT END OF YEAR	$ 99,716	$ 244,5
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:		
Cash paid during the year for:		
Interest	$ 312,293	$ 44,6

NON-CASH FINANCING ACTIVITIES:

COMPENSATION SATISFIED BY ISSUANCE OF COMMON STOCK	$ --	$ --
COMMON STOCK ISSUED IN SATISFACTION OF LIABILITIES	$ 650,563	$ 40,0
RECLASSIFICATION OF DERIVATIVE LIABILITIES UPON CONVERSION OF DEBT	$ 368,800	$ --
RECLASSIFICATION OF EQUITY INSTRUMENTS TO LIABILITIES UPON ISSUANCE OF CONVERTIBLE DEBT	$ 288,900	$ --

The accompanying notes are an integral part of these financial statements

WATER CHEF, INC.

(A Development Stage Company Commencing January 1, 2002)

NOTES TO FINANCIAL STATEMENTS

1. DESCRIPTION OF BUSINESS

Water Chef, Inc. (the "Company"), is a Delaware Corporation currently engaged in the design, marketing and sale of water dispensers and purification equipment both in and outside the United States. The Company's corporate headquarters is in Glen Head, NY.

2. BASIS OF PRESENTATION AND CONTINUED OPERATIONS

Basis of Presentation

The Company discontinued its water cooler and filtration operations in November 2001. As a result, the Company has refocused its efforts on raising capital and developing markets for its proprietary technology. Therefore, for financial purposes, the Company has determined that it has re-entered the development stage commencing January 1, 2002. The Company's statements of operations, stockholders' deficiency and cash flows for the year ended December 31, 2006 represent the financial information cumulative, from inception/commencement, required by Statement of Financial Accounting Standards ("SFAS") No. 7, "Development Stage Enterprises."

Going Concern

The accompanying financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America, which contemplate continuation of the Company as a going concern and the realization of assets and the satisfaction of liabilities in the normal course of business. The carrying amounts of assets and liabilities presented in the financial statements do not purport to represent realizable or settlement values. The Company incurred a net loss of $2,072,917 and $1,168,328 for the years ended December 31, 2006 and 2005, respectively. The Company has a working capital

deficit and a stockholders' deficiency of approximately $3,123,219 and $3,625,725 at December 31, 2006, respectively. These conditions raise substantial doubt about the Company's ability to continue as a going concern.

Management's plans with respect to these matters include restructuring its existing debt and raising additional capital through future issuances of stock and/or debt. The accompanying financial statements do not include any adjustments that might result from the outcome of this uncertainty.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Patents and Trademarks - Patents and trademarks are amortized ratably over 9 to 14 years. The Company assesses the carrying value of its patents for impairment each year. Based on its assessments, the Company did not incur any impairment charges for the years ended December 31, 2006 and 2005, respectively.

Stock-Based Compensation -
Effective January 1, 2006, the Company adopted SFAS 123R which replaces SFAS 123, "Accounting for Stock-Based Compensation" and supersedes Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees." SFAS 123R requires all share-based payments to employees, including grants of employee stock options, to be recognized in the financial statements based on their fair values. Pro forma disclosure is no longer an alternative to financial statement recognition. The adoption of this standard had no effect on operations for the year ended December 31, 2006 as the Company did not issue any options during the period and the Company did not have any vested or unvested options outstanding.

The Black-Scholes option valuation model is used to estimate the fair value of the options granted. The model includes subjective input assumptions that can materially affect the fair value estimates. The model was developed for use in estimating the fair value of traded options or warrants that have no vesting restrictions and that are fully transferable. For example, the expected volatility is estimated based on the most recent historical period of time equal to the weighted average life of the options granted. In management's opinion, this valuation model does not necessarily provide a reliable single measure of the fair value of its employee stock options. During the year ended December 31, 2006 and 2005, the Company did not issue any employee stock options.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Prior to the adoption of SFAS 123R, the Company applied the intrinsic-value-based method of accounting prescribed by APB 25 and related interpretations, to account for its stock options to employees. Under this method, compensation cost was recorded only if the market price of the underlying stock on the date of grant exceeded the exercise price. As permitted by SFAS 123, the Company elected to continue to apply the intrinsic-value-based method of accounting described above, and adopted only the disclosure requirements of SFAS 123. The fair-value-based method used to determine

historical pro forma amounts under SFAS 123 was similar in most respects to the method used to determine stock-based compensation expense under SFAS 123R.

In December 2002, the Financial Accounting Standards Board ("FASB") issued SFAS No. 148, "Accounting for Stock-Based Compensation - Transition and Disclosure - an amendment of FASB Statement No. 123." SFAS No. 148 amends SFAS No. 123, "Accounting for Stock-Based Compensation," to provide alternative methods of transition for a voluntary change to the fair value based method of accounting for stock-based employee compensation. In addition, SFAS No. 148 amends the disclosure requirements of SFAS No. 123 to require prominent disclosures in both annual and interim financial statements about the method of accounting for stock-based employee compensation and the effect of the method used on reported results.

The Company did not incur stock based compensation for issuance of options during the year ended December 31, 2005. As such, the pro forma net loss is identical to the net loss as reported in the financial statements of operations. Revenue Recognition - Revenues are recognized when product is shipped, title passes and collectibility is reasonably assured. Allowances for estimated bad debts, sales allowances and discounts are provided when such sales are recorded.

Inventories - Inventories consists of finished goods and are stated at the lower of cost or market utilizing the first-in, first-out method. As of December 31, 2006, the Company had no inventory on hand.

Shipping and Handling Costs - Shipping and handling costs are expensed as incurred as part of cost of sales. These costs were deemed to be immaterial during each of the reporting periods.

Advertising Costs - Advertising costs are expensed as incurred. Advertising costs, which are included in selling, general and administrative expenses, were diminimus for the years ended December 31, 2006 and 2006, respectively.

Income Taxes - Income taxes are accounted for under SFAS No. 109, "Accounting for Income Taxes," which is an asset and liability approach that requires the recognition of deferred tax assets and liabilities for the expected future tax consequences of events that have been recognized in the Company's financial statements or tax returns. Valuation allowances are established when necessary to reduce deferred assets to the amounts expected to be realized.

Loss Per Share - Basic loss per share was computed using the weighted average number of outstanding common shares. Diluted loss per share includes the effect of dilutive common stock equivalents from the assumed exercise of options, warrants and convertible preferred stock. Common stock equivalents were excluded from the computation of diluted loss per share since their inclusion would be anti-dilutive. Total shares issuable upon the exercise of options, warrants and the conversion of preferred stock and convertible debt for the years ended December 31, 2006 and 2005, were 12,719,202 and 21,270,105 respectively.

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

WATER CHEF, INC.

(A Development Stage Company Commencing January 1, 2002)

NOTES TO FINANCIAL STATEMENTS
Continued

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Fair Value of Financial Instruments - The carrying amounts of the financial instruments reported in the balance sheet approximate their fair market value due to the short-term maturities of these instruments. The fair value of the Company's long-term debt is estimated using quoted market prices and estimated rates which would be available to the Company for debt with similar terms.

Impairment of Long-Lived Assets - In the event that facts and circumstances indicate that the cost of an asset may be impaired, an evaluation of recoverability would be performed. If an evaluation is required, the estimated future undiscounted cash flows associated with the asset would be compared to the asset's carrying amount to determine if a write-down to fair value is required.

Research and Development - Research and development costs consist of expenditures incurred during the course of planned research and investigation aimed at the discovery of new knowledge, which will be useful in developing new products or processes. The Company expenses all research and development costs as incurred. There were no research and development costs incurred during the years ended December 31, 2006 and 2005, respectively.

Deferred Financing Costs - Costs incurred in conjunction with the convertible promissory notes have been capitalized and will be amortized over the term of the notes.

Recent Accounting Pronouncements

In June 2005, the Financial Accounting Standards Board ("FASB") published SFAS No. 154, "Accounting Changes and Error Corrections - a Replacement of APB Opinion No. 20 and FASB No. 3" ("SFAS 154"). SFAS 154 establishes new standards on accounting for changes in accounting principles. Pursuant to the new rules, all such changes must be accounted for by retrospective application to the financial statements of prior periods unless it is impracticable to do so. SFAS 154 completely replaces Accounting Principles Bulletin No. 20 and SFAS 3, though it carries forward the guidance in those pronouncements with respect to accounting for changes in estimates, changes in the reporting entity, and the correction of errors. The requirements in SFAS 154 are effective for accounting changes made in fiscal years beginning after December 15, 2005. The adoption of this pronouncement did not have an impact on the Company's financial position, results of operations, or cash flows.

In June 2006, the FASB ratified EITF Issue No. 05-1, "Accounting for the Conversion of an Instrument That Becomes Convertible upon the Issuer's Exercise of a Call Option" ("EITF No. 05-1"), which indicates that no gain or loss should be recognized upon the conversion of an instrument that becomes convertible as a result of an issuer's exercise of a call option pursuant to the original terms of the instrument. EITF No. 05-1 became effective for annual or interim periods beginning after June 28, 2006. The adoption of this pronouncement did not have an impact on the Company's financial position, results of operations, or cash flows.

In June 2005, the FASB ratified EITF Issue No. 05-2, "The Meaning of `Conventional Convertible Debt Instrument" in EITF Issue No. 00-19, "Accounting for Derivative Financial Instruments Indexed to, and Potentially Settled in, a

Company's Own Stock" ("EITF No. 05-2"), which addresses when a convertible debt instrument should be considered "conventional" for the purpose of applying the guidance in EITF No. 00-19. EITF No. 05-2 also retained the exemption under EITF No. 00-19 for conventional convertible debt instruments and indicated that convertible preferred stock having a mandatory redemption date may qualify for the exemption provided under EITF No. 00-19 for conventional convertible debt if the instrument's economic characteristics are more similar to debt than equity.

EITF No. 05-2 became effective for new instruments entered into and instruments modified in periods beginning after June 29, 2005. The Company has applied the requirements of EITF No. 05-2 since the required implementation date. The adoption of this pronouncement did not have an impact on the Company's financial position, results of operations, or cash flows.

WATER CHEF, INC.

(A Development Stage Company Commencing January 1, 2002)

NOTES TO FINANCIAL STATEMENTS
Continued

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

In September 2005, the FASB ratified EITF Issue No. 05-7, "Accounting for Modifications to Conversion Options Embedded in Debt Instruments and Related Issues" ("EITF No. 05-7"), which addresses whether a modification to a conversion option that changes its fair value affects the recognition of interest expense for the associated debt instrument after the modification and whether a borrower should recognize a beneficial conversion feature, not a debt extinguishment, if a debt modification increases the intrinsic value of the debt (for example, the modification reduces the conversion price of the debt). EITF No. 05-7 became effective for the first interim or annual reporting period beginning after December 15, 2005. The Company adopted EITF No. 05-7 as of the beginning of the Company's interim reporting period that began on January 1, 2006. The adoption of this pronouncement did not have an impact on the Company's financial position, results of operations, or cash flows.

In September 2005, the FASB ratified EITF Issue No. 05-8, "Income Tax Consequences of Issuing Convertible Debt with a Beneficial Conversion Feature" ("EITF No. 05-8"), which addresses the treatment of convertible debt issued with a beneficial conversion feature as a temporary difference under the guidance in SFAS 109. In addition, deferred taxes recognized for a temporary difference of debt with a beneficial conversion feature should be recognized as an adjustment of additional paid-in capital. Entities should apply the guidance in EITF No. 05-8 in the first interim or annual reporting period that begins after December 15, 2005. Its provisions should be applied retrospectively under the guidance in SFAS 154 to all convertible debt instruments with a beneficial conversion feature accounted for under the guidance in EITF No. 00-27 "Application of EITF Issue No. 98-5 "Accounting for Convertible Securities with Beneficial Conversion Features or Contingently Adjustable Conversion Ratios." The Company has applied the requirements of EITF No. 05-8 to all previously existing convertible debt instruments with a beneficial conversion feature and will apply the requirements of EITF No. 05-8 for all new convertible debt instruments with a beneficial conversion feature. The adoption of this pronouncement for new convertible debt instruments with a beneficial conversion feature did not have an impact on the Company's financial position, results of operations or cash flows.

In February 2006, the FASB issued SFAS 155, "Accounting for Certain Hybrid

Financial Instruments - an amendment of FASB Statements No. 133 and 140" ("SFAS 155"). SFAS 155 resolves issues addressed in SFAS 133 Implementation Issue No. D1, "Application of Statement 133 to Beneficial Interests in Securitized Financial Assets." The requirements in SFAS 155 are effective for all financial instruments acquired or issued after the beginning of an entity's first fiscal year that begins after September 15, 2006. The adoption of this pronouncement is not expected to have an impact on the Company's financial position, results of operations, or cash flows.

In July 2006, the FASB released Interpretation No. 48, "Accounting for Uncertainty in Income Taxes--an interpretation of FASB Statement No. 109" ("FIN 48"), which clarifies the accounting and reporting for uncertainty in income tax law. FIN 48 prescribes a comprehensive model for the financial statement recognition, measurement, presentation and disclosure of uncertain tax positions taken or expected to be taken in income tax returns. The provisions of FIN 48 are effective after December 15, 2006. Earlier adoption is permitted as of the beginning of an enterprise's fiscal year, provided the enterprise has not yet issued financial statements, including financial statements for any interim period for that fiscal year. The cumulative effects, if any, of applying FIN 48 will be recorded as an adjustment to accumulated deficit as of the beginning of the period of adoption. The adoption of this pronouncement is not expected to have an impact on the financial position, results of operations, or cash flows of the Company.

In September 2006, the FASB issued SFAS No. 157, "Fair Value Measurements" ("SFAS 157"). SFAS 157 defines fair value, establishes a framework for measuring fair value in accordance with accounting principles generally accepted in the U.S., and expands disclosures about fair value measurements. SFAS 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007, with earlier application encouraged. Any cumulative effect will be recorded as an adjustment to the opening accumulated deficit balance, or other appropriate component of equity. The adoption of this pronouncement is not expected to have an impact on the Company's financial position, results of operations, or cash flows.

In September 2006, the SEC staff issued Staff Accounting Bulleting ("SAB") No. 108, Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements ("SAB 108"). SAB 108 was issued in order to reduce the diversity in practice in how public companies quantify misstatements of financial statements, including misstatements that were not material to prior years' financial statements. SAB 108 is effective for fiscal year 2007. The adoption of this pronouncement is not expected to have an impact on the Company's financial position, results of operations, or cash flows.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

In October 2005, the FASB issued FSP FAS 123(R)-2, "Practical Accommodation to the Application of Grant Date as Defined in FASB Statement No. 123(R)", which provides clarification of the concept of mutual understanding between employer

and employee with respect to the grant date of a share-based payment award. This FSP provides that a mutual understanding of the key terms and conditions of an award shall be presumed to exist on the date the award is approved by management if the recipient does not have the ability to negotiate the key terms and conditions of the award and those key terms and conditions will be communicated to the individual recipient within a relatively short time period after the date of approval. This guidance was applicable upon the initial adoption of SFAS 123(R). The adoption of this pronouncement did not have an impact on the Company's financial position, results of operations, or cash flows.

In February 2007, the FASB issued SFAS No. 159, "The Fair Value Option for Financial Assets and Financial Liabilities" ("SFAS 159"). SFAS 159 provides companies with an option to report selected financial assets and liabilities at fair value. The objective of SFAS 159 is to reduce both complexity in accounting for financial instruments and the volatility in earnings caused by measuring related assets and liabilities differently. Generally accepted accounting principles have required different measurement attributes for different assets and liabilities that can create artificial volatility in earnings. The FASB has indicated it believes that SFAS 159 helps to mitigate this type of accounting-induced volatility by enabling companies to report related assets and liabilities at fair value, which would likely reduce the need for companies to comply with detailed rules for hedge accounting. SFAS 159 also establishes presentation and disclosure requirements designed to facilitate comparisons between companies that choose different measurement attributes for similar types of assets and liabilities.

SFAS 159 does not eliminate disclosure requirements included in other accounting standards, including requirements for disclosures about fair value measurements included in SFAS 157 and SFAS No. 107, "Disclosures about Fair Value of Financial Instruments." SFAS 159 is effective for the Company as of the beginning of fiscal year 2009 The adoption of this pronouncement is not expected to have an impact on the Company's financial position, results of operations or cash flows.

In December 2006, the FASB approved FASB Staff Position (FSP) No. EITF 00-19-2, "Accounting for Registration Payment Arrangements" ("FSP EITF 00-19-2"), which specifies that the contingent obligation to make future payments or otherwise transfer consideration under a registration payment arrangement, whether issued as a separate agreement or included as a provision of a financial instrument or other agreement, should be separately recognized and measured in accordance with SFAS No. 5, "Accounting for Contingencies". FSP EITF 00-19-2 also requires additional disclosure regarding the nature of any registration payment arrangements, alternative settlement methods, the maximum potential amount of consideration and the current carrying amount of the liability, if any. The guidance in FSP EITF 00-19-2 amends FASB Statements No. 133, "Accounting for Derivative Instruments and Hedging Activities", and No. 150, "Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity", and FASB Interpretation No. 45, "Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others", to include scope exceptions for registration payment arrangements.

FSP EITF 00-19-2 is effective immediately for registration payment arrangements and the financial instruments subject to those arrangements that are entered into or modified subsequent to the issuance date of this FSP, or for financial statements issued for fiscal years beginning after December 15, 2006, and interim periods within those fiscal years, for registration payment arrangements entered into prior to the issuance date of this FSP. The adoption of this pronouncement is not expected to have an impact on the Company's financial position, results of operations or cash flows.

EITF Issue No. 05-4 "The Effect of a Liquidated Damages Clause on a Freestanding Financial Instrument Subject to EITF Issue No. 00-19, `Accounting for Derivative

Financial Instruments Indexed to, and Potentially Settled in, a Company's Own Stock'" ("EITF No. 05-4") addresses financial instruments, such as stock purchase warrants, which are accounted for under EITF No. 00-19 that may be issued at the same time and in contemplation of a registration rights agreement that includes a liquidated damages clause. The consensus of EITF No. 05-4 has not been finalized.

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WATER CHEF, INC.

(A Development Stage Company Commencing January 1, 2002)

NOTES TO FINANCIAL STATEMENTS
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4. PATENTS AND TRADEMARKS

Patents and trademarks as of December 31, 2006 consist of the following:

Patents	$ 24,500
Trademarks	1,555
Total cost	26,055
Accumulated amortization	(10,652)
Patents and Trademarks, Net	$ 15,403

Amortization expense for the years ended December 31, 2006 and 2005 was $1,854 and $1,854, respectively. The following table presents the Company's estimate for amortization expense for each of the five succeeding years and thereafter.

2007	$ 1,854
2008	1,854
2009	1,854
2010	1,854
2011	1,854
2012 and thereafter	6,133
	$ 15,403

5. NOTES PAYABLE

Notes payable and accrued interest at December 31, 2006 consists of the following:

(a)	$ 187,470
(b)	635,933
(c)	167,453
Total	$ 990,856

(a): These are unsecured notes bearing interest ranging from 10% to 15% per

annum, with no specific due date for repayment. The amount due on these notes, inclusive of $104,249 interest is $187,470 at December 31, 2006. No demands for repayment have been made by the note holder.

(b) In April 2001, the Company issued a $400,000 promissory note at an interest rate of 2% per month. In consideration for the issuance of this note, 500,000 shares of the Company's common stock were issued to the note holder and a $74,000 debt discount was recorded and fully amortized in the year ended December 31, 2001. The principal balance and accrued interest was payable on September 1, 2001. The Company did not make such payment and was required to issue an additional 100,000 penalty shares of its common stock to the note holder. The Company recorded additional interest expense of $12,300 related to the issuance of these penalty shares. The amount due on this note, inclusive of $235,933 in interest, is $635,933 at December 31, 2006.

(c) In November 2000, the Company entered into a Convertible Promissory Note agreement, whereby the Company may be advanced a maximum of $300,000. The Company was advanced the following: $100,000 in November 2000, $50,000 in December 2000 and $50,000 in January 2001. No further cash advances were made to the Company. The Convertible Promissory Note agreement also called for the payment of $100,000 of Company expenses. The advances bear interest at 10% per annum and were to have been repaid as of January 15, 2002. A maximum of 6,000,000 shares could have been issued upon conversion had the full $300,000 been advanced. As of December 31, 2006, the balance of the convertible promissory note principal was $167,453 inclusive of interest in the amount of $3,082.

6. CONVERTIBLE PROMISSORY NOTES

In November 2005, the Company entered into a Convertible Promissory Note agreement for $250,000 which included 430,000 warrants, which are exercisable at $0.14 per share and have a life of three years. The warrants carry a cashless exercise provision. The Convertible Promissory Note bore interest at a rate of 8% per annum and matured in March 2006.

The note included certain conversion features as follows:

- convertible at any time after the maturity date, at the option of the holder,
- convertible at 85% of the average of the three 3 lowest closing bid prices for the common stock, for the ten trading days ending on the trading day immediately before the conversion date.

The Convertible Promissory Note agreement required the Company to file a registration statement no later than sixty business days from the date of the agreement for no less than the amount of subscribed shares, and to cause the registration statement relating to the registrable securities to become effective the earlier of five business days after notice from the Securities and Exchange Commission that the registration statement may be declared effective,

or (b) one hundred twenty days.

The Convertible Promissory Note agreement included a liquidated damages clause, which stipulates if the registration statement is not filed by the filing date or declared effective by the effective date, then upon failure of either event the subscriber shall be entitled to liquidated damages, payable in cash, in the sum of one percent (1%) of the principal amount of the Note:

a. for each 30 day period after the filing date that transpires until the date that the Company files the registration statement, and
b. for each 30 day period after the effective date that transpires until such date as the registration statement is declared effective.

The gross proceeds of $250,000 were recorded net of a discount of $188,000. The debt discount consisted of $47,200 related to the warrants and $140,800 related to the embedded conversion option. The warrants and the embedded conversion option were accounted for under EITF issue No. 00-19 "Accounting for Derivative Financial Instruments Indexed to, and Potentially Settled in, a Company's Own Stock" and EITF 05-4, View A "The effect of a Liquidated Damages Clause on a Freestanding Financial Instrument." Due to certain factors and the liquidated damage provision in the registration rights agreement, the Company determined that the embedded conversion option and the warrants are derivative liabilities.

Accordingly, the warrants and the embedded conversion option were marked to market through earnings at the end of each reporting period. The Company determined that the value of the registration rights was deemed to be de minimis and the related registration statement became effective in January 2006. The warrants and the conversion option were valued using the Black-Scholes valuation model. For the year ended December 31, 2006, the Company reflected a loss of $186,600 representing the change in the value of the warrants and conversion option. During the year ended December 31, 2006, the Company charged to interest expense $112,800 for the accretion of the debt discount.

During the year ended December 31, 2006, the Company issued 3,012,547 shares of common stock for the settlement of the debt and accrued interest. As a result of the conversion the Company reclassified to equity $368,800 of the derivative liabilities.

This Convertible Promissory Note was secured by 4,000,000 shares held by an officer of the Company. At the date of conversion the officer was released from the security interest.

On October 17, 2006, the Company entered into a Convertible Promissory Note for proceeds of $300,000. The loan has a stated interest rate of 8% per annum and matures on February 17, 2007. The Company issued a warrant for 882,352 shares of the Company's common stock, exercisable at $0.085 per share and has a life of three years. The warrant has a cashless exercise provision. The note and accrued interest is convertible at any time after the maturity date into shares of the Company's common stock at a conversion price equal to the current market price multiplied by eighty-five percent.

The Convertible Promissory Note agreement requires the Company to file a registration statement no later than thirty business days from the date of the agreement and no less than the amount of subscribed shares, and to cause the registration statement relating to the registrable securities to become effective the earlier of five business days after notice from the Securities and Exchange Commission that the registration statement may be declared effective, or one hundred twenty days.

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NOTES TO FINANCIAL STATEMENTS
Continued

6. CONVERTIBLE PROMISSORY NOTES (continued)

The Convertible Promissory Note agreement included a liquidated damages clause, which stipulates if the registration statement is not filed by the filing date or declared effective by the effective date, then upon failure of either event the subscriber shall be entitled to liquidated damages, payable in cash, in the sum of one percent (1%) of the principal amount of the Note:

(a) for each 30 day period after the filing date the transpires until the date that the Company files the registration statement, and
(b) for each 30 day period after the effective date that transpires until such date as the registration statement is declared effective.

The Company accounted for the above transaction in accordance with EITF issue No. 00-19 "Accounting for Derivative Financial Instruments Indexed to, and Potentially Settled in, a Company's Own Stock." The Company has determined that there is an embedded conversion option of the warrants and derivative liabilities. Accordingly, the warrants and the embedded conversion option are recorded at fair market value and marked to market through earnings at the end of each reporting period.

The gross proceeds of $300,000 were recorded net of a discount of $174,200. The debt discount consisted of $12,800 related to the warrants and $161,400 related to the embedded conversion option. The warrants and the embedded conversion option were accounted for under EITF issue No. 00-19 "Accounting for Derivative Financial Instruments Indexed to, and Potentially Settled in, a Company's Own Stock" and EITF 05-4, View A "The Effect of a Liquidated Damages Clause on a Freestanding Financial Instrument." Due to certain factors and the liquidated damage provision in the registration rights agreement, the Company determined that the embedded conversion option and the warrants are derivative liabilities.

Accordingly, the warrants and the embedded conversion option will be marked to market through earnings at the end of each reporting period. The Company determined that the value of the registration rights was deemed to be de minimis and the related registration statement became effective in January 2007. The warrants and the conversion option are valued using the Black-Scholes valuation model. For the year ended December 31, 2006, the Company reflected a gain of $85,900 representing the change in the value of the warrants and conversion option. During the year ended December 31, 2006, the Company charged to interest expense $104,520 for the accretion of the debt discount.

The Convertible Promissory Note was secured by 4,000,000 shares held by an officer of the Company.

Under the terms of the note the Company is currently in default, subsequent to the year end the Company issued 948,670 shares of common stock for the settlement of $100,000 of principal and $3,249 of accrued interest. The Company plans to issue additional shares of common stock for the settlement of the remaining principal an accrued interest.

Under accounting guidance provide by EITF 00-19, the conversion price of the convertible promissory note did not have a determinable number of shares the note could be settled in. As a result, previously granted warrants as well as the embedded conversion option of the Series F Convertible Preferred Stock were required to be reclassified from equity and presented as a derivative liability in the amount of $288,900. Accordingly, the warrants, options and conversion

option will be marked to market through earnings at the end of each reporting period. For the year ended December 31, 2006, the Company incurred an additional charge of $33,200 representing the change in the fair value of the warrants and embedded conversion option of the Series F Convertible Preferred Stock.

7. LOANS PAYABLE - STOCKHOLDER

At December 31, 2006, the Company has been obligated to its Chief Executive Officer who is also a significant stockholder for loans and advances made to the Company totaling $372,781, plus accrued interest of $152,956. These advances were accruing interest ranging from 6% to 12% per annum. The loans have no repayment terms and the stockholder has agreed not to demand payment until January 1, 2008 at the earliest. The Company reported the obligation as a long-term liability on the balance sheet. In January 2007, in conjunction with the resignation of the Chief Executive Officer (Note 15) these loans plus accrued interest were forgiven.

8. COMMON STOCK ISSUED

On March 14, 2006, at the Company's annual meeting of its common, Series A Preferred, Series C Preferred, Series D Preferred, Series F Preferred stockholders (together the "Stockholders"), voting as a single class, voted and approved a proposal to amend the Certificate of Incorporation to increase the Company's authorized capital stock from 200,000,000 shares to 350,000,000 shares, consisting of 340,000,000 shares of common stock and 10,000,000 shares of preferred stock.

8. COMMON STOCK ISSUED (continued)

During the year ended December 31, 2006, the Company recorded the following transactions:

a. Cash

During the year ended December 31, 2006, the Company raised $568,000 through the sale of 7,869,230 shares of common stock

b. Services

During the year ended December 31, 2006, the Company issued 866,666 shares of common stock for services for a value of $62,499.

On May 18, 2006, the Company granted 4,000,000 warrants to a consultant for past services. The warrants fully vested the date of the grant, have a life of 3 years and are exercisable at $0.10 per share. The Company incurred a stock based compensation charge of $464,000.

On May 24, 2006, the Company granted 2,500,000 warrants to two directors for past services. The warrants fully vested on the date of the grant, have a life of 3 years and are exercisable at $0.15 per share. The Company incurred a stock

based compensation charge of $241,200.

c. Conversion of preferred stock into common stock

During year ended December 31, 2006, the Company issued to various parties 1,866,720 shares of its common stock in connection with the conversion of 46,668 shares of preferred stock.

Subsequent to December 31, 2006, the Company issued to various parties 113,920 shares of its common stock in connection with the conversion of 2,848 shares of preferred stock.

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WATER CHEF, INC.

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NOTES TO FINANCIAL STATEMENTS
Continued

8. COMMON STOCK ISSUED (continued)

d. Settlement of debt

During year ended December 31, 2006, the Company issued 6,595,881 shares of common stock for debt and accrued interest of $650,563.

9. PREFERRED STOCK

The Company is authorized to issue 10,000,000 shares of $.001 par value preferred stock, issuable in series with rights, preferences, privileges and restrictions as determined by the board of directors.

At December 31, 2006, outstanding preferred shares were as follows:

	Authorized Shares	Outstanding Shares	Par Value	Current Annual Dividend Requirement	Total Dividend Arrearage	Dividend Arrearage Per Share	Liquidatio Preferenc (including dividend arrearage
Series A	400,000	52,500	$ 53	$ 52,500	$ 622,600	$ 11.86	$1,147,60
Series D	2,000,000	93,000	93	55,800	585,000	6.29	1,119,75
Series F	1,000,000	43,417	43	--	189,871	--	--
		188,917	$ 189	$ 108,300	$1,397,471		$2,267,35

Series A:

The Series A preferred stock provides for a 10% cumulative dividend, based on the $10 per share purchase price, payable annually in the Company's common stock or cash, at the Company's option. The Series A preferred stock is not convertible, and is redeemable solely at the Company's option at a price of $11

per share plus accrued dividends. The Series A preferred stockholders have voting rights equal to common stockholders.

In the event of the liquidation, dissolution or winding up of the Company, whether voluntary or involuntary, holders of the Series A preferred stock are entitled to receive out of the assets of the Company the sum of $10.00 per share of Series A preferred stock then outstanding, plus a sum equal to all dividends (whether or not earned or declared) on such shares accrued and unpaid thereon to the date of final payment or distribution, before any payment or distribution upon dissolution, liquidation or winding up shall be made on any series or class of capital stock ranking junior to Series A preferred stock as to such payment or distribution.

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NOTES TO FINANCIAL STATEMENTS
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9. PREFERRED STOCK (continued)

Series C:

During the year ended December 31, 2002, the Company sold Series C 15% Convertible Preferred stock at $1.00 per share. These shares convert in one year. All dividends are cumulative and are payable in shares of the Company's common stock valued at the then-current market price per share, or upon conversion, whichever is earlier. The conversion rate for shares, and accrued dividends payable, is 33.33 shares of common for each $1.00 of preferred stock and dividends payable, or $0.03 for each share of common stock. The Series C Preferred stockholders have voting rights equal to the common stockholders. The Series C preferred stock has no stated rights in the assets of the Company upon liquidation. During 2002, the Company sold 125,000 shares of Series C preferred stock. For each share of preferred stock purchased, the buyers also receive the right to receive an additional 33.33 shares of common stock upon conversion, as the market value of the stock was $0.015 at issuance.

Series D:

The Series D preferred stock provides for a 12% cumulative dividend, based on the $5 per share purchase price, payable semi-annually in the Company's common stock or cash, at the Company's option. The Series D preferred stock is not convertible, and is redeemable solely at the Company's option at a price of $5.75 per share plus accrued dividends. The Series D Preferred stockholders have voting rights equal to the common stockholders.

In the event of the liquidation, dissolution or winding up of the Company, whether voluntary or involuntary, holders of the Series D preferred stock are entitled to receive out of the assets of the Company the sum of all dividends (whether or not earned or declared) on such shares accrued and unpaid thereon to the date of final payment or distribution, before any payment or distribution upon dissolution, liquidation or winding up shall be made on any series or class of capital stock ranking junior to Series D preferred stock as to such payment

or distribution.

Series F:

In April 2003, management authorized the Company to raise up to $550,000 through a private placement by issuing 10% two-year convertible preferred instruments. The preferred, designated as Series F, and provided for one million shares in total and can be convertible into shares of Water Chef's common stock at such time as the stockholders of the corporation approve an increase in the authorized capital stock of the corporation, which occurred on June 4, 2004. All dividends are cumulative and are payable in shares of the Company's common stock valued at the then current market price per share, at the time of maturity, or upon conversion, whichever is earlier. The conversion rate for shares and accrued dividends payable is 40 shares of common for each share of preferred stock. The Series F convertible preferred stockholders have voting rights equal to the common stockholders. The Series F convertible preferred stock has no stated rights in the assets of the Company upon liquidation.

Although there was a discount upon the issuance of all of the Series F preferred stock in accordance with EITF 98-5, a security is not yet convertible if certain contingencies exist which are dependent upon the occurrence of a future event outside the control of the security holder. In this case, the shares can only be converted into common stock after the stockholders of the Company approve an increase in the authorized capital stock of the corporation. In accordance with EITF 98-5, any beneficial conversion (discount) feature is measured at the commitment date, but will not be recognized as an adjustment to earnings until the contingency is resolved, (the date the increase in shares are approved). In June 2004, the Company voted and approved a proposal to amend the Certificate of Incorporation to increase the Company's authorized capital stock from 100,000,000 to 200,000,000 shares, consisting of 190,000,000 shares of common stock and 10,000,000 shares of preferred stock. During June 2004, the Company recorded the deferred contingent beneficial conversion adjustment of $2,072,296 as a deemed dividend since the contingency was resolved.

In connection with Series F Preferred Stock conversions, the Company recorded dividends of $42,401 and $66,436 for each of the years ended December 31, 2006 and 2005, respectively.

10. STOCK OPTION, STOCK APPRECIATION RIGHTS AND WARRANT GRANT PLAN

The Company's President and Director were issued in the aggregate 6,000,000 options to purchase common stock of the Company in January 2004. The total options granted may be converted to common stock at an exercise price of $0.25 and expire in five years. Those options were converted to stock appreciation rights [the "Conversion"] in November 2004. The Conversion consisted of 5,000,000 stock appreciation rights granted to the President which vest over 5 years and 1,000,000 stock appreciation rights granted to the director which vest over 2 years.

In March 1997, the Company, in connection with Bridge Loans for $375,000 issued warrants to purchase 2,500,001 shares of common stock at $.15 per share. These

warrants had a life of five years and were to have expired in March 2002. For the year ended December 31, 2000, a total of 333,334 common shares were issued upon the exercise of a like number of warrants, for net proceeds of $50,000. Of the remaining 2,166,667 un-exercised warrants at March 2002, a total of 1,666,667 warrants had their lives extended for an additional two years until March 2004 and then later for another twelve months until March 2005. The remaining balance of 500,000 warrants was not extended and, accordingly, they have expired. The extension of the exercise date was part of a settlement that the Company had reached with certain debenture holders that had brought legal action against the Company. In June 2005, the Company extended for the second time the life of the warrants for one year. The Company recorded an additional charge of $74,700, which has been included in the statements of operations.

The fair value of each stock option, or warrant granted, is estimated on the date of grant using the Black-Scholes option-pricing model. During the year ended December 31, 2005, the Company granted 433,000 warrants in connection with the Convertible Promissory Note and 883,000 warrants during the year ended December 31, 2006.

The following tables illustrate the Company's warrant issuances and balances outstanding as of, and during the years ended December 31, 2006 and 2005:

	Shares Underlying Warrants	Weighted Average Exercise Price
Outstanding at December 31, 2004	1,666,667	$ 0.15
Granted	433,000	0.14
Expired	-	-
Exercised	-	-
Outstanding at December 31, 2005	2,099,667	$ 0.15
Granted	7,382,352	0.12
Expired	(1,666,667)	(0.15)
Exercised	-	-
Outstanding at December 31, 2006	7,815,352	$ 0.12

The following is additional information with respect to the Company's warrants as of December 31, 2006:

WARRANTS OUTSTANDING				WARRANTS EXERCISABLE	
Exercise Price	Number of Outstanding Warrants	Weighted Average Remaining Contractual Life	Weighted Average Exercise Price	Number of Exercisable Warrants	Weighted Average Exercise Price
$ 0.09	882,352	2.8 years	$0.09	882,352	$0.09
$ 0.10	4,000,000	2.4 years	$0.10	4,000,000	$0.10
$ 0.14	433,000	1.8 years	$0.14	433,000	$0.14
$ 0.15	2,500,000	2.4 years	$0.15	2,500,000	$0.15
	7,815,352			7,815,352	

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11. LEASES

The Company's lease for its administrative facilities located in Glen Head, New York is on a month to month basis. This lease terminated on March 31, 2006.

Rent expense, for the years ended December 31, 2006 and 2005 was $31,935 and $30,189, respectively.

The Company entered into a month to month lease beginning April 2, 2007 in Melville, New York for its administrative facilities.

12. LITIGATION

On July 14, 2006, Funding Group, Inc. filed a complaint with the Supreme Court of the State of New York in New York County seeking damages due to an alleged breach of contract related to a $25,000 loan made by the plaintiff to the Company. On October 11, 2006, the Company filed a counter claim against Funding Group, Inc. with the Supreme Court of the State of New York. The Company believes the complaint is without merit and intends to vigorously defend itself in these actions, and believes that the eventual outcome of these matters will not have a material adverse effect on the Company. However, the ultimate outcome of these matters cannot be determined at this time.

13. INCOME TAXES

The Company accounts for income taxes under SFAS No. 109, Accounting for Income Taxes. SFAS No. 109 requires the recognition of deferred tax assets and liabilities for both the expected impact of differences between the financial statements and tax basis of assets and liabilities, and for the expected future tax benefit to be derived from tax loss and tax credit carry forwards. SFAS No. 109 additionally requires the establishment of a valuation allowance to reflect the likelihood of realization of deferred tax assets.

For the year ended December 31, 2006 and 2005, no provision for income taxes has been provided for, as a result of continued net operating losses. The Company is subject to certain state and local taxes based on capital. The state and local taxes based on capital were immaterial for each of the years ended December 31, 2006 and 2005.

The effective tax rate differs from the statutory rate of 34% due to the increase of the valuation allowance.

The Company has net operating loss carry-forwards for federal income tax purposes totaling approximately $23,600,000 at December 31, 2006. These carry-forwards expire between the years 2009 through 2026. Utilization of these loss carry-forwards may be limited under Internal Revenue Code Section 382. The deferred tax asset arising from the net operating loss carry-forwards has been offset by a corresponding valuation allowance.

The valuation allowance primarily relates to the federal and state net operating losses for which utilization in future periods is uncertain. The ultimate

realization of deferred tax assets is dependent upon the generation of future taxable income during the periods in which those temporary differences become deductible. The Company considers projected future taxable income and tax planning strategies in making this assessment. Based on projections for future taxable income over the periods that the deferred tax assets are deductible, the Company believes it is more likely than not that the Company will not realize the benefits of these deductible differences in the near future and therefore a full valuation allowance of $8,750,000 is provided. The valuation allowance increased approximately $1,800,000 during 2006 related to increased net operating losses.

14. MAJOR CUSTOMERS

During the year ended December 31, 2006, the Company sold two systems to one customer and recognized revenues of $115,000. During the year ended December 31, 2005, the Company sold five systems to two customers and recognized revenue of $260,000.

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15. COMMITMENTS AND CONTINGENCIES

In January 1, 2004, the Company entered into a 5 year employment agreement with its Chief Executive Officer ("Employee"). The Company agreed to pay to the Employee for the services to be rendered a base salary at an annual rate of three hundred and fifty thousand dollars. The Company granted to its employee a five-year option for 5,000,000 shares of the Company's outstanding common stock for an option price of $.25 per share. The option will vest in fifty equal, consecutive monthly increments of 100,000 shares each on the first day of each month beginning with January of 2004 and ending with February of 2008. Those options were converted to stock appreciation rights in November 2004. As of December 31, 2006, approximately $471,600 was owed and is included on the balance sheet as part of accrued compensation. On January 29, 2007, the Company's Chief Executive Officer resigned and surrendered his Stock Appreciation Rights, any severance under his employment agreement, returned 20,000,000 shares of common stock, forgave $525,738 of notes payable and accrued interest and relinquished his rights to approximately $471,600 of unpaid and accrued salary. The Company will reclassify to equity in the first quarter ended 2007 approximately $471,600 for the relinquishment of his rights to the unpaid and accrued salary and $525,738 notes payable and accrued interest. The return of the shares will be recorded as a retirement and cancellation of the common stock. The cancellation of the stock appreciation rights did not have an accounting impact.

On March 9, 2004, the Company extended for two additional years the consulting agreement with a director. The Company agreed to increase his monthly payment to $10,000 per month. The Company also gave him the right to purchase one million shares of the Company's common stock at a price of $0.25 per share, such right to vest at the rate of 50% per year. Those options were converted to stock appreciation rights in November 2004. For each of the years ended December 31, 2006 and 2005, the Company incurred a charge of $60,000 and $120,000 respectively, which has been included in the statement of operations as part of

selling general and administrative costs. In addition, the director earned approximately $25,000 of director fees. On February 12, 2007 the director resigned from the Board of Directors and waived his rights to any accrued compensation owed to him by the Company. The Company will reclassify the debt of approximately $330,000 during the first quarter ended 2007 to equity for the relinquishment of his rights to the unpaid and accrued consulting and director fees.

16. CREDIT RISK

The Company maintains its cash in accounts with major financial institutions in the United States. From time to time, these balances may exceed the amounts of insurance provided on such deposits. As of December 31, 2006, there were no uninsured balances.

17. SUBSEQUENT EVENTS

In January 2007, David Conway resigned as President and Chief Executive Officer of the Corporation, and as a member of the Board of Directors. In February 2007, Marshall Sterman resigned as a member of the Board of Directors.

In January 2007, Leslie J. Kessler was appointed as President of the Company. In connection with her employment, she is to receive a salary of $9,000 per month. In addition, Ms. Kessler will be issued 2,000,000 shares of the Company's common stock and a warrant to purchase 2,000,000 shares of the Company's common stock. The Company plans to implement a performance-based cash incentive plan for Ms. Kessler as well. The complete terms of the employment agreement have not been finalized.

In February 2007, Ms. Kessler was appointed Chief Executive Officer and was elected to the Board of Directors.

In January 2007, Dr. Ronald W. Hart, Chairman of the Company's Board of Scientific Advisors, was appointed to the Board of Directors of Water Chef, Inc.

Effective with David Conway's resignation, John J. Clarke became Chairman of the Board, and upon Marshall Sterman's resignation he became Chairman of the Audit and Compensation Committees of the Board.