

TANKLESS SYSTEMS WORLDWIDE INC  
Form 10QSB  
August 15, 2005

U.S. SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

**FORM 10-QSB**

(Mark One)

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

**For the quarterly period ended June 30, 2005**

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

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

*COMMISSION FILE NUMBER: 000-27549*

**TANKLESS SYSTEMS WORLDWIDE, INC .**

(Exact name of Company as specified in its charter)

**NEVADA**

**88-0362112**

Edgar Filing: TANKLESS SYSTEMS WORLDWIDE INC - Form 10QSB

(State or other jurisdiction of  
incorporation or organization)

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

7650 E. Evans Road, Suite C, Scottsdale, Arizona 85260

(Address of principal executive offices)

(Zip Code)

Company's telephone number: (480) 609-7575

-----

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 Company was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes  No

APPLICABLE ONLY TO CORPORATE ISSUERS

State the number of shares outstanding of each of the issuer's classes of common equity. As of August 12, 2005  
15,037,238, \$0.001 par value.

Transitional Small Business Disclosure Format (check one): YES  NO

Index

Page

Number

PART I FINANCIAL INFORMATION

ITEM 1. Financial Statements (unaudited)

Report of Independent Registered Public Accounting Firm

3

Consolidated Balance Sheets as of June 30, 2005

and December 31, 2004

4 -5

Consolidated Statements of Operations for the six months

ended June 30, 2005 and 2004

6

Consolidated Statements of Stockholders' Equity cumulative

from December 31, 2000 to June 30, 2005

7-9

Consolidated Statements of Cash Flows for the six months

ended June 30, 2005 and 2004

10

Notes to Financial Statements

11-21

ITEM 2. Managements Discussion and Analysis of Financial Condition  
and Results of Operations/Plan of Operation

22

ITEM 3. Controls and Procedures

25

PART II OTHER INFORMATION

ITEM 1. Legal Proceedings

26

ITEM 2. Change in Securities and Use of Proceeds

27

ITEM 3. Defaults Upon Senior Securities

27

ITEM 4. Submission of Matters to Vote of Security Holders

28

ITEM 5. Other Information

28

ITEM 6. Exhibits

28

SIGNATURES

28

PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

Report of Independent Registered Public Accounting Firm

To the Board of Directors and Audit Committee

Tankless Systems Worldwide, Inc.

We have reviewed the accompanying consolidated interim balance sheets of Tankless Systems Worldwide, Inc., as of June 30, 2005, and December 31, 2004 and the associated consolidated statements of operations, stockholders' equity and cash flows for the three and six month periods ended June 30, 2005 and June 30, 2004. These interim financial statements are the responsibility of the Company's management.

We conducted our review in accordance with the standards of the Public Company Accounting Oversight Board (United States). A review of interim financial information consists principally of applying analytical procedures and making inquiries of persons responsible for financial and accounting matters. It is substantially less in scope than an audit conducted in accordance with the standards of the Public Company Accounting Oversight Board, the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, we do not express such an opinion.

Based on our review, we are not aware of any material modifications that should be made to the accompanying interim financial statements for them to be in conformity with U.S. generally accepted accounting principles.

Shelley International, CPA

Mesa, Arizona, U.S.A.

August 12, 2005

Tankless Systems Worldwide, Inc.

CONSOLIDATED BALANCE SHEETS

	<u>ASSETS</u>	
	June 30 2005 (Unaudited)	December 31, 2004
<b>CURRENT ASSETS</b>		
Cash	\$ 39,744	\$ 18,690
Accounts Receivable, Net	108,342	110,721
Inventory at Cost	118,373	76,131
Prepaid Expenses	2,782	2,782
 Total Current Assets	 269,241	 208,324
 EQUIPMENT, NET	 43,926	 62,282
<b>OTHER ASSETS</b>		
Patents and Software, Net	43,576	43,778
Investment in Subsidiary	250,000	250,000
Other Receivables	75,527	
Deposits	7,514	7,514
 Total Other Assets	 376,617	 301,292
 Total Assets	 \$ 689,784	 \$ 571,898

The accompanying notes are an integral part of these statements





Tankless Systems Worldwide, Inc.

CONSOLIDATED BALANCE SHEETS, continued**LIABILITIES AND STOCKHOLDERS' EQUITY**

## LIABILITIES

Accounts Payable	\$ 877,693	\$ 618,155
Other Payables	25,330	76,125
Notes Payable	1,814,758	1,952,258
Accrued Interest Payable	111,483	100,891
Related Party Payable	60,000	
Customer Deposits	168,544	120,368
Total Liabilities	3,057,808	2,867,797

## STOCKHOLDERS' EQUITY

Common Stock authorized is 100,000,000 shares at \$0.001par value. Issued and outstanding on June 30, 2005 is 14,753,713 shares, December 31, 2004 is 13,125,977 shares.	14,754	13,126
Paid in Capital	1,775,166	1,122,648
Subscriptions Receivable	(37,500)	(112,500)
Retained (Loss)	(4,120,444)	(3,319,173)
Total Stockholders' Equity	(2,368,024)	(2,295,899)

## TOTAL LIABILITIES AND

STOCKHOLDERS EQUITY	\$ 689,784	\$ 571,898
---------------------	------------	------------

The accompanying notes are an integral part of these statements

## Tankless Systems Worldwide, Inc.

**CONSOLIDATED STATEMENTS OF OPERATIONS****(Unaudited)**

	Three Months Ended		Six Months Ended	
	June 30		June 30	
	2005	2004	2005	2004
<b>INCOME</b>				
Product Sales	\$ 96,534	\$ 61,235	\$ 151,561	\$ 216,440
Other Income	6,264	80	6,264	159
Total Income	102,798	61,315	157,825	216,599
Less Cost of Goods Sold	15,004	46,232	37,826	146,735
Gross Income	87,794	15,083	119,999	69,864
<b>EXPENSES</b>				
Legal and Professional	36,802	19,384	56,081	69,646
General and Administrative	350,848	290,117	504,693	547,772
Research and Development	50,770	(19,750)	209,688	750
Advertising	-	924	813	10,292
Loss on Sale of Assets	-			
Depreciation	9,179		18,357	7,032
Amortization	6,613		13,227	2,133
Interest Expense	53,537	13,154	118,411	48,721
Total Expenses	507,749	303,829	921,270	686,346
Net (Loss) before Income Taxes	(419,955)	(288,746)	(801,271)	(616,482)
Income Tax Expense				
<b>NET (LOSS)</b>	<b>\$ (419,955)</b>	<b>\$ (288,746)</b>	<b>\$ (801,271)</b>	<b>\$ (616,482)</b>

Edgar Filing: TANKLESS SYSTEMS WORLDWIDE INC - Form 10QSB

Basic and diluted (loss) per share	\$ (0.03)	\$ (0.02)	\$ (0.06)	\$ (0.05)
Weighted Average Number of Common				
Shares Outstanding	13,383,051	11,657,120	13,383,051	11,657,120

The accompanying notes are an integral part of these statements

**Tankless Systems Worldwide, Inc.**  
**CONSOLIDATED STATEMENT OF STOCKHOLDERS EQUITY**  
**For the period December 31, 2000 to June 30, 2005**

	Common Stock Shares	Amount	Paid in Capital	Subscriptions Receivable	Accumulated (Loss)	Total Equity
<b>Balance December 31, 2000</b>	580,000	\$ 580	\$ 333,920	\$ -	\$ (828,006)	\$ (493,506)
Common Shares issued for Services	52,500	53	52,447			52,500
Contribution to Capital			24,265			24,265
Common Shares issued to retire Convertible Note and accrued Interest Net (Loss)	60,000	60	187,022		(120,900)	187,082 (120,900)
<b>Balance December 31, 2001</b>	692,500	693	597,654	-	(948,906)	(350,559)
Common Shares issued for cash	104,778	105	96,895			97,000
Common Shares issued for services	455,800	455	110,045			110,500
Common Shares issued for prepaid service	162,500	163	16,087			16,250
Common Shares issued for						

proposed business acquisition	5,525,944					
Common Shares issued to retire convertible note and accrued Interest	60,000	60	200,670			200,730
Common Shares issued to retire debt	22,500	22	23,272			23,294
Net (Loss)					(1,154,438)	(1,154,438)
<b>Balance December 31, 2002</b>	7,024,022	1,498	1,044,623	-	(2,103,344)	(1,057,223)

(Continued on  
following page)

The accompanying notes are an integral part of these statements

**Tankless Systems Worldwide, Inc**  
**CONSOLIDATED STATEMENT OF STOCKHOLDERS EQUITY, Continued**  
**For the period December 31, 2000 to June 30, 2005**

	Common Stock Shares	Common Stock Amount	Paid in Capital	Subscriptions Receivable	Accumulated (Loss)	Total Equity
<b>Balance December 31, 2002</b>	7,024,022	1,498	1,044,623	-	(2,103,344)	(1,057,223)
Common Shares cancelled and retained earnings adjustment for termination of business acquisition	(5,525,944)				852,261	852,261
Common Shares cancelled for unused prepaid service	(162,500)	(163)	(16,087)			(16,250)
Common Shares issued to retire Debt in the amount of \$27,205	49,645	50	27,815			27,865
Common Shares issued for services	1,622,855	1,623	317,572			319,195
Common Shares issued for business acquisition including purchase of (Negative) Capital	8,366,378	8,366	241,634			250,000
Common Stock Options			(1,125,661)			(1,125,661)



Edgar Filing: TANKLESS SYSTEMS WORLDWIDE INC - Form 10QSB

issued for services			6,300			6,300
Net (Loss)					(366,913)	(366,913)
<b>Balance December 31, 2003</b>	11,374,456	11,374	496,196	-	(1,617,996)	(1,110,426)
Common Shares issued for services	1,337,500	1,338	387,418			388,756
Common Shares issued to retire Debt and interest of \$91,281	172,354	172	91,109			91,281
Common Shares issued for cash through exercise of warrants	66,667	67	16,600			16,667
Common Shares cancelled in acquisition settlement	(2,075,000)	(2,075)	2,075			-
Common Stock Options issued for services			19,000			19,000
Common Stock issued for subscriptions receivable	2,250,000	2,250	110,250	(112,500)		-
Net (Loss)					(1,701,177)	(1,701,177)
<b>Balance December 31, 2004</b>	13,125,977	\$13,126	\$ 1,122,648	\$ (112,500)	\$ (3,319,173)	\$ (2,295,899)

(Continued on following page)

The accompanying notes are an integral part of these statements



**Tankless Systems Worldwide, Inc.****CONSOLIDATED STATEMENT OF STOCKHOLDERS EQUITY, Continued****For the period December 31, 2000 to June 30, 2005**

	Common Stock Shares	Common Stock Amount	Paid in Capital	Subscriptions Receivable	Accumulated (Loss)	Total Equity
<b>Balance December 31, 2004</b>	13,125,977	\$ 13,126	\$ 1,122,648	\$ (112,500)	\$ (3,319,173)	\$ (2,295,899)
Common Shares issued for services	774,201	774	183,927			184,701
Common Shares issued for Cash	540,909	541	296,959			297,500
Common Shares issued to retire Debt and accumulated interest in the amount of \$171,945	312,626	313	171,632			171,945
Service received on subscriptions receivable				75,000		75,000
Net (Loss)					(801,271)	(801,271)
<b>Balance June 30, 2005</b>	14,753,713	\$ 14,754	\$ 1,775,166	\$ (37,500)	\$ (4,120,444)	\$ (2,368,024)

The accompanying notes are an integral part of these statements



## Tankless Systems Worldwide, Inc.

**CONSOLIDATED STATEMENTS CASH FLOWS**

(Unaudited)

	Six Months Ended June 30	
	2005	2004
Operating Activities		
Net (Loss)	\$ (801,271)	\$ (616,482)
Common Share Options issued for service		6,000
Shares issued for services rendered.	184,701	232,550
Shares issued to retire debt and interest.	171,945	39,034
Amortization of intangible assets.	202	2,133
Depreciation Expense.	18,356	7,032
Original Issue Discount	23,947	(92,750)
Changes in assets and liabilities:		
Inventory	(42,242)	7,123
Accounts Receivable	(73,148)	(13,430)
Prepaid Expense		(24,622)
Accrued Interest Payable	(13,355)	13,788
Accounts Payable	208,743	(62,058)
Notes Payable	(157,500)	30,000
Subscription Receivable	75,000	
Customer Deposits	48,176	(24,024)
Net Cash Provided by Operating Activities	(356,446)	(495,706)
Investing Activities		
Purchase of Patents and Software		(11,502)
Purchase of Equipment	-	(22,163)
Net Cash (Used) by Investing Activities	-	(33,665)
Financing Activities		
Proceeds Received from sale of stock	297,500	16,667
Principal Received on convertible debentures	20,000	550,738

Edgar Filing: TANKLESS SYSTEMS WORLDWIDE INC - Form 10QSB

Principal received from related party loan	60,000	
Cash Provided by Financing Activities	377,500	567,405
Net Increase/(Decrease) in Cash	21,054	38,034
Cash, Beginning of Period	18,690	412
Cash, End of Period	\$ 39,744	\$ 38,446
Supplemental Information:		
Taxes	\$ -	\$ -
Interest	\$ 119,690	\$ 48,721

The accompanying notes are an integral part of these statements

**Tankless Systems Worldwide, Inc.**

**NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS**

**June 30, 2005 and December 31, 2004**

**Note 1. THE COMPANY AND ITS SIGNIFICANT ACCOUNTING POLICIES**

**The Company**

Tankless Systems Worldwide, Inc., a Nevada corporation (Company), was originally organized on November 23, 1993 as Amexan, Inc., and then on June 1, 1998 the name was changed to Nostalgia Motorcars, Inc. On June 11, 2002, the Company changed its name to Elution Technologies, Inc., and on June 4, 2003, it changed its name to Tankless Systems Worldwide, Inc.

On November 7, 2003, the Company acquired Envirotech Systems Worldwide, Inc. (Envirotech), a private Arizona corporation, as a wholly owned subsidiary. The acquisition was accounted for using purchase accounting. The purchase was made in a one-for-one stock exchange of 8,366,778 shares of the Company's common stock for all of the issued and outstanding shares of Envirotech. For more details of this acquisition see Note 2.

Envirotech was organized December 9, 1998 and has a limited history of operations. The initial period of its existence involved research and development of a line of electronic, tankless water heaters. The first sales of its products occurred in calendar year 2000.

With the acquisition of Envirotech, the Company is in the business of designing, developing, manufacturing and marketing several models of an electronic, tankless water heaters.

During January 2004 the Company organized ION Tankless, Inc. an Arizona Corporation as a wholly owned subsidiary. ION is organized to do research, development and marketing of new tankless technologies.

On January 30, 2005 the Company organized Valeo Industries, Inc. a Nevada Corporation as a wholly owned subsidiary. Valeo will manufacture and distribute new products arriving from ongoing research and development.

**Use of Estimates and Assumptions**

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America (GAAP) requires management to make estimates and assumptions that affect the reported amounts and the disclosure of contingent amounts in the Company's financial statements and the accompanying notes. Actual results could differ from those estimates.

The accompanying balance sheets of June 30, 2005, and December 31, 2004, and the related statements of operations, stockholders' equity, and cash flows for the periods ended June 30, 2005 and 2004, consolidate the activity of the Company for all reported periods with the activity of its subsidiary Envirotech from January 1, 2004 to June 30, 2005; its subsidiary ION from inception (January 2004) to June 30, 2005 and its subsidiary Valeo from inception (January 2005) to June 30, 2005.



### **Financial Instruments**

The carrying value of the Company's financial instruments, consisting of cash, accounts payable, accrued liabilities, and accrued interest payable approximate their fair value due to the short-term maturity of such instruments. The carrying value of convertible debt approximates fair value as the related interest rate is variable and approximates market rates. Unless otherwise noted, it is management's opinion that the Company is not exposed to significant interest, currency or credit risks arising from these financial instruments.

### **Research and Development**

The Company expensed product research and development costs as they are incurred. The Company had one product with variations in capacity based on the flow of electricity. With the organization of its new subsidiary ION, the Company continues to expense research and development costs as incurred in developing additional products based on new technology.

### **Marketing Strategy**

The Company sells directly to individuals through the Internet, through distributorships, and through high volume retailers. The Company periodically advertises on cable television stations, trade shows and trade magazines and maintains an extensive website.

### **Revenue Recognition**

The Company usually sells its units through credit card sales to individuals and normally does not maintain receivables. However, the Company does sell on credit to distributors. Credit card sales are recognized upon shipment of the product to the customer. All shipments are FOB shipping point. Sales to distributorships are sold FOB shipping point with 30-day terms on receivables.

### **Accounts Receivable**

## Edgar Filing: TANKLESS SYSTEMS WORLDWIDE INC - Form 10QSB

Accounts receivable is recorded when an order is received from a distributor. An allowance for doubtful accounts was set up based on the actual rate of uncollected accounts. Net accounts receivable is as follows:

### Period Ended

6/30/05

12/31/04

Accounts Receivable

\$115,298

\$69,774

Employee Advances

47,903

Less Allowance for Doubtful Accounts

(6,956)

(6,956)

Net Accounts Receivable

\$108,342

\$110,721

### **Advertising**

Advertising expense included the cost of sales brochures, print advertising in trade publications, displays at trade shows and maintenance of an Internet site. Advertising is expensed when incurred. Advertising expense for the three months ended June 30, 2005 and March 31, 2004 is \$813 and \$9,368 respectively.

### **Inventory**

The Company contracts with a third party to manufacture the units and is not billed for nor obligated for any work-in-process. The Company only supplies certain parts and materials and is then billed for completed products.

Parts and material inventory is stated at the lower of cost (first-in, first-out) or net realizable value.

**Equipment**

Equipment is depreciated using the straight-line method over the estimated useful lives, which range from two to seven years. Fixed assets consist of the following:

Period Ended

6/30/05

12/31/04

Tooling, machinery, furniture

and fixtures

\$192,861

\$192,861

Less: Accumulated depreciation

(148,935)

(130,579)

Total

\$ 43,926

\$ 62,282

**Patents**

Patent and software costs include direct costs of obtaining patents. Costs for new patents are capitalized and amortized over the estimated useful lives of seventeen years and software over five years.

Period Ended

6/30/05

12/31/04

Patents and heater software

\$147,300

\$134,274

Accumulated Amortization

(103,724)

(90,496)

Net Patents and Heater Software

\$43,576

\$43,778

### **Earnings per Share**

The basic (loss) per share is calculated by dividing the Company's net income available to common shareholders by the weighted average number of common shares during the year.

The Company has no potentially dilutive securities outstanding at the end of the statement periods. Therefore, the basic and diluted earnings (loss) per share are presented on the face of the statement of operations. All outstanding warrants were either exercised or cancelled and convertible debt is anti-dilutive.

### **Stock Based Compensation**

The Company accounts for its stock based compensation based upon provisions in SFAS No. 123, *Accounting for Stock-Based Compensation*. In this statement stock based compensation is divided into two general categories, based upon who the stock receiver is, namely: employees/directors and non-employees/directors. The employees/directors category is further divided based upon the particular stock issuance plan, namely compensatory and non-compensatory. The employee/directors non-compensatory securities are recorded at the sales price when the stock is sold. The compensatory stock is calculated and recorded at the securities' fair value at the time the stock is

given. SFAS 123 also provides that stock compensation paid to non-employees be recorded with a value which is based upon the fair value of the services rendered or the value of the stock given, whichever is more reliable. The common stock paid to non-employees was valued at the value of the services rendered.

**Warranty and Right of Return**

Upon the sale of a system, the Company gives a 30-day money back guarantee less a 6% restocking charge. After the 30 days the Company gives an additional five years warranty on replacement of parts. The tank chamber is warranted not to leak for 20 years.

**Note 2.**

ACQUISITION OF SUBSIDIARY

On November 7, 2003, the Company acquired Envirotech Systems Worldwide, Inc. a private Arizona corporation (Envirotech), as a wholly owned subsidiary. The purchase was made in a one-for-one stock exchange of 8,366,778 shares of the Company's common stock for all of the issued and outstanding shares of Envirotech.

At the time of purchase the balance sheet of Envirotech was as follows:

Total Assets

\$ 328,900

Liabilities

1,451,561

Stockholders (Negative) Equity

(1,125,661)

Total Liabilities and Stockholders' Equity

\$ 328,900

Per the purchase agreement Tankless acquired goodwill/client files valued at \$250,000 and the negative equity of \$1,125,661. The purchased client files will assist in future marketing and the Company considers the goodwill value unchanged.

**Note 3.**

NOTES PAYABLE AND CAPITAL LEASE OBLIGATIONS:

Edgar Filing: TANKLESS SYSTEMS WORLDWIDE INC - Form 10QSB

During the year ended December 31, 2004, the Company received \$1,075,000 through private placements to accredited investors. The investor receives a one-year debenture with an interest rate of 10% per year, payable, quarterly. Additionally, the investor receives one (1) share of the Company's restricted common stock for each Two Dollars (\$2.00) of debentures purchased. The principle and unpaid interest is convertible to common stock at the rate of one share of stock for every \$1.00 outstanding. During 2004 a \$30,000 and a \$50,000 note including associated interest were converted to common stock.

Notes payable and capital lease obligations consist of the following:

For Period Ended

6/30/05

12/31/04

Convertible Notes, Unsecured, Matured March 2001 bear 12.5% Interest, principal and interest convertible into one common share and one warrant at 75% of the average closing price over the 10-day period prior to conversion. Warrants have expired and notes have not been converted and are in default.

\$100,000

\$100,000

Convertible Notes, Unsecured, Matured one-year from issue date, bear 10% Interest payable quarterly, principal and interest convertible into one common share for each outstanding \$1.00. Thirty-six notes



are outstanding that were issued between January 23

and December 14, 2004. Aggregate Amount:

867,500

1,025,000

Convertible Notes, Unsecured, Matured one-year  
from issue date, bear 10% Interest payable quarterly,  
principal and interest convertible into one common  
share for each outstanding \$1.00. Six notes  
are outstanding that were issued January 7, 2005.

Aggregate Amount:

20,000

Aggregate amount of principle and interest  
on notes payable of Subsidiary Envirotech  
listed in Chapter 11 Bankruptcy

827,258

846,523

Total Notes Payable

1,814,758

1,971,523

Accrued Interest Payable

111,483

81,626

Total Notes and Interest Payable

\$1,926,241

\$2,053,149

**Note 4.**

STOCKHOLDERS EQUITY

As of June 30, 2005, the Company has 100,000,000 shares of common stock authorized at a par value of \$0.001. On June 30, 2005 and December 31, 2004 common stock issued and outstanding were 14,753,713 and 13,125,977 shares respectively.

On July 25, 2002, the Company adopted an employee stock incentive plan setting aside 1,000,000 shares of the Company's common stock for issuance to officers, employees, directors and consultants for services rendered or to be rendered. The proposed maximum offering price of such shares is \$1.00 per share.

A compensation committee appointed by the Board of Directors who shall have the right to grant awards or stock options administers the plan.

On October 15, 2002, the Company filed a Registration on Form S-8 with the Securities Exchange Commission covering the 1,000,000 shares provided by this plan, at a maximum offering price of \$1.00 per share.

As of December 31, 2002, 540,000 shares of common stock have been issued at \$0.10 per share under this plan leaving a balance of 460,000 shares available under the plan, all of which were subsequently issued in 2003.

On August 19, 2003, the Company adopted an employee stock incentive plan setting aside 960,000 shares of the Company's common stock for issuance to officers, employees, directors and consultants for services rendered or to be rendered. The proposed maximum offering price of such shares is \$1.00 per share.

A compensation committee appointed by the Board of Directors who shall have the right to grant awards or stock options administers the plan.

Edgar Filing: TANKLESS SYSTEMS WORLDWIDE INC - Form 10QSB

On September 12, 2003, the Company filed a Registration on Form S-8 with the Securities Exchange Commission covering the 960,000 shares provided by this plan, at a maximum offering price of \$1.00 per share.

From the date of adoption of the Plan to November 7, 2003, the Company issued all of the shares covered by this Plan.

On December 1, 2003, the Company adopted an employee stock incentive plan setting aside 165,000 shares of the Company's common stock for issuance to officers, employees, directors and consultants for services rendered or to be rendered. The proposed maximum offering price of such shares is \$1.00 per share.

A compensation committee appointed by the Board of Directors who shall have the right to grant awards or stock options administers the plan.

On December 19, 2003, the Company filed a Registration on Form S-8 with the Securities Exchange Commission covering the 165,000 shares provided by this plan, at a maximum offering price of \$1.00 per share.

As of March 31, 2004, the Company has issued all of the shares covered by the 2003 Stock Incentive Plan adopted by the Company on December 1, 2003

On December 23, 2004, the Company accepted the return and cancellation of 2,075,000 common shares in settlement of action taken by the company against prior shareholders of Envirotech in connection with claims made during its purchase.

On March 24, 2005, the Company adopted an employee stock incentive plan setting aside 500,000 shares of the Company's common stock for issuance to officers, employees, directors and consultants for services rendered or to be rendered. The proposed maximum offering price of such shares is \$1.00 per share.

A compensation committee appointed by the Board of Directors who shall have the right to grant awards or stock options administers the plan.

On March 30, 2005, the Company filed a Registration on Form S-8 with the Securities Exchange Commission covering the 500,000 shares provided by this plan, at a maximum offering price of \$1.00 per share.

As of June 30, 2005, the Company has issued 124,201 shares covered by the 2005 Stock Incentive Plan adopted by the Company on March 24, 2005.

The Company was initially capitalized November 30, 1993 with the issue of 500,000 shares for \$5,000 and at December 31, 2004 had 13,125,977 common shares outstanding. Since December 31, 2004 the Company has issued 774,201 common shares for services valued at \$184,701, 540,909 common shares for \$297,500 cash, and 312,626 shares in satisfaction of total principal and interest on notes payable in the amount of \$171,945.

**Warrants:** No warrants are currently outstanding.

**Stock Options:** In connection with the acquisition of Envirotech Systems Worldwide, Inc., the Company issued immediately vested stock options on October 29, 2003 to one of the principal shareholders of Envirotech. He was granted the right to purchase 300,000 restricted common shares at \$0.55 per share until October 29, 2004 (extended to December 31, 2004 and now expired).

On February 11, 2004 the company granted 5-year stock options to purchase 600,000 shares of restricted common stock at \$0.50 per share to consultants assisting in company operations. Using a discounted stock price of \$0.43, exercise price of \$0.50, 5-year option, risk-free rate of 4.1% and a volatility rate of .038 the value of these options is calculated at \$0.03 using the Black-Scholes model. The aggregate value of 600,000 options is \$18,000.

Edgar Filing: TANKLESS SYSTEMS WORLDWIDE INC - Form 10QSB

On December 31, 2004 options to purchase 100,000 restricted common shares were granted as part of a settlement agreement. The options are immediately vested and the holder has the right to purchase 100,000 restricted shares at an exercise price of \$0.55 per share and will expire in one year (December 31, 2005). Using a discounted stock price of \$0.44, exercise price of \$0.55, 1-year option, risk-free rate of 4.1% and a volatility rate of .038 the value of these options is calculated at \$0.01 using the Black-Scholes model. The aggregate value of 100,000 options is \$1,000.

Outstanding stock options are as follows:

Shares

Balance, December 31, 2003

300,000

Granted

700,000

Canceled

(300,000)

Balance, June 30, 2005

700,000

**Note 5.**

**INCOME TAXES:**

The Company provides for income taxes under Statement of Financial Accounting Standards No. 109, *Accounting for Income Taxes*. SFAS No. 109 requires the use of an asset and liability approach in accounting for income taxes. Deferred tax assets and liabilities are recorded based on the differences between the financial statement and tax bases of assets and liabilities and the tax rates in effect currently.

Edgar Filing: TANKLESS SYSTEMS WORLDWIDE INC - Form 10QSB

SFAS No. 109 requires the reduction of deferred tax assets by a valuation allowance if, based on the weight of available evidence, it is more likely than not that some or all of the deferred tax assets will not be realized. In the Company's opinion, it is uncertain whether they will generate sufficient taxable income in the future to fully utilize the net deferred tax asset. Accordingly, a valuation allowance equal to the deferred tax asset has been recorded. The total deferred tax asset is \$735,555, as of 12/31/04, which is calculated by multiplying a 22% estimated tax rate by the cumulative NOL of \$3,343,434. The total valuation allowance is a comparable \$735,555.

Year Ended December 31

2004

2003

2002

Deferred Tax Asset

374,259

\$80,722

\$253,976

Valuation Allowance

(374,259)

(80,722)

(253,976)

Current Taxes Payable

0.00

0.00

0.00

Income Tax Expense

\$ 0.00



\$ 0.00

\$ 0.00

Below is a chart showing the estimated federal net operating losses and the years in which they will expire.

Year

Amount

Expiration

2001

120,900

2021

2002

1,154,438

2022

2003

366,919

2023

2004

1,701,177

2024

Total

\$3,343,434



**Note 6.**

LEASES AND OTHER COMMITMENTS:

The Company occupies space leased by Envirotech. The lease extends to June 30, 2006 and contains a 120 day escape clause. The numbers shown below assume that the Company will remain in its current office space.

Year 1

Year 2

Year 3

Year 4

Year 5

Office Lease

25,435

25,435

25,435

25,435

25,435

**Note 7.**

GOING CONCERN

Listed below are some of the challenges which the Company is facing, and why these raise a question as to the Company's ability to continue as a going concern. Also described are management's plans to turn the Company around.

### **Company's Challenges**

The Company has a substantial deficit in retained earnings from losses for the previous years. Its subsidiary, Envirotech has not been able to generate enough sales to cover annual expenses and has survived only by raising funds. The Company must continue to raise funds in the near future to survive. Management has been successful in the past in raising these funds. There is no assurance that management can continue to find investors to cover the losses generated.

### **Management's Plans**

Management feels that the trends are encouraging because its subsidiary has increased sales each year of operation. Advertising will continue through the printed media, cable television and the Internet. As new homebuilders become aware of the product it will be included in original house plans. Management has placed the unit in large retail stores which is driving much of the upward sales trend.

On February 1, 2004, the company initiated its management transition plan as a result of its acquisition of its subsidiary Envirotech. The Company entered into several consulting agreements to assist in day-to-day operations and provide financial, management and other consulting services to the Company and its subsidiaries. These persons will serve as part of the management team during the periods of their engagement and will perform a variety of services to include:

1.

The evaluation of potential business opportunities

2.

The business operations and management

3.

The development of business strategies

4.

Raising public and private capital

Pursuant to these agreements, the company has committed to issue 700,000 shares of common stock and has granted options to purchase an additional 600,000 restricted shares at a price of \$0.50 per share at any time prior to February

1, 2009. All stock issued or to be issued is subject to the limitations imposed by Rule 144. Management believes these individuals and entities are crucial to the future of the Company and that the consideration paid for their services is fair and reasonable.

**Note 8.**

PENDING LITIGATION

The Company's subsidiary Envirotech is currently a defendant in a patent infringement lawsuit. Management feels that this action is baseless and that the Company will prevail. No contingent liability has been recorded nor contemplated at this point. Action has been stayed through Bankruptcy Petition.

In 2004 Envirotech was named in three separate lawsuits for unpaid legal and consulting fees totaling \$268,000. Envirotech believed it had meritorious defenses to each of these suits. On April 14, 2004, Envirotech settled one of these suits, considering it a nuisance claim. In connection with that settlement, Envirotech reimbursed the plaintiff for alleged out-of-pocket expenses and the Company issued 10,000 shares of common stock, restricted under Rule 144, to the plaintiff on the basis of a loan from the Company to Envirotech. In the other two suits Envirotech elected not to spend funds to defend the action and judgments were granted in the aggregate amount of approximately \$155,500. These judgments have been stayed through Bankruptcy Petition (see Note 9). Any settlements of these suits will be reflected as a charge in the year of the settlement.

On August 13, 2004, the Company filed a verified complaint in the United States District Court in and for the District of Arizona against certain key individuals who were principles of Envirotech prior to its acquisition. The action alleged against various defendants, Breach of Fiduciary Duty, Aiding and Abetting Breach of Fiduciary Duty, Breach of Contract, Breach of Implied Covenant of Good Faith and Fair Dealing, Fraud and Intentional Misrepresentation, Conspiracy to Defraud, Arizona Securities Fraud, Federal Securities Fraud, Negligent Misrepresentation, Misappropriation of Trade Secrets and Confidential Business Information, Conversion/Embezzlement, Intentional Interference with Business Relations and Prospective Economic Advantage, Unjust Enrichment, and Promissory Estoppel. The Company sought relief, which included, but was not limited to, Damages, Constructive Trust, Rescission and Injunctive Relief. This action has been settled with the return and cancellation of 2,075,000 shares of common stock and the agreement of the defendants to other conditions, including agreements not to compete for specified periods of time.

**Note 9.**

SUBSIDIARY BANKRUPTCY

On August 6, 2004, Envirotech Systems Worldwide, Inc., a wholly-owned subsidiary of the Company, filed for protection under Chapter 11 of the United States Bankruptcy Code in Phoenix, Arizona. Envirotech was acquired by the Company in November 2003 in a stock-for-stock, one-for-one transaction, and has been held and operated by the Registrant as an operating subsidiary. With the exception of a guarantee to one critical supplier in the current amount

of approximately \$42,500, the Registrant has not assumed any liability for the obligations of Envirotech. As of the date of the filing of the Chapter 11 Bankruptcy Petition, Envirotech had liabilities of approximately \$1.6 million. Several creditors not related to the supply of parts or the assembly of products have obtained judgments against Envirotech and an action was pending in the U.S. District Court, Southern District of Texas, alleging patent infringement. The filing of the Bankruptcy Petition has stayed all creditors and suits.

**Note 10.**

**THE EFFECT OF RECENTLY ISSUED ACCOUNTING STANDARDS**

Below is a listing of the most recent accounting standards SFAS 146-150 and their effect on the Company.

**Statement No. 150**

*Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity* (Issued 5/03)

This Statement establishes standards for how an issuer classifies and measures certain financial instruments with characteristics of both liabilities and equity.

**Statement No. 151**

*Inventory Costs*-an amendment of ARB No. 43, Chapter 4 (Issued 11/04)

This statement amends the guidance in ARB No. 43, Chapter 4, *Inventory Pricing*, to clarify the accounting for abnormal amounts of idle facility expense, freight, handling costs, and wasted material (spoilage). Paragraph 5 of ARB 43, Chapter 4, previously stated that under some circumstances, items such as idle facility expense, excessive spoilage, double freight and re-handling costs may be so abnormal as to require treatment as current period charges. This Statement requires that those items be recognized as current-period charges regardless of whether they meet the criterion of so abnormal. In addition, this Statement requires that allocation of fixed production overheads to the costs of conversion be based on the normal capacity of the production facilities.

**Statement No. 152**

*Accounting for Real Estate Time-Sharing Transactions* (an amendment of FASB Statements No. 66 and 67)

This Statement amends FASB Statement No. 66, *Accounting for Sales of Real Estate*, to reference the financial accounting and reporting guidance for real estate time-sharing transactions that is provided in AICPA Statement of Position (SOP) 04-2, *Accounting for Real Estate Time-Sharing Transactions*.

This Statement also amends FASB Statement No. 67, *Accounting for Costs and Initial Rental Operations of Real Estate Projects*, states that the guidance for (a) incidental operations and (b) costs incurred to sell real estate projects does not apply to real estate time-sharing transactions. The accounting for those operations and costs is subject to the guidance in SOP 04-2.

**Statement No. 153**

*Exchanges of Non-monetary Assets* (an amendment of APB Opinion No. 29)



The guidance in APB Opinion No. 29, *Accounting for Non-monetary Transactions*, is based on the principle that exchanges of non-monetary assets should be measured based on the fair value of the assets exchanged. The guidance in that Opinion, however, includes certain exceptions to the principle. This Statement amends Opinion 29 to eliminate the exception for non-monetary exchanges of similar productive assets and replaces it with a general exception for exchanges of non-monetary assets that do not have commercial substance. A non-monetary exchange has commercial substance if the future cash flows of the entity are expected to change significantly as a result of the exchange.

The adoption of these new Statements is not expected to have a material effect on the Company's current financial position, results or operations, or cash flows.

**Note 10.**

**SUBSEQUENT EVENTS**

On December 24, 2004 the Company issued 2,250,000 shares of common stock for \$112,500 subscription receivable in anticipation of executing various consulting agreements. These shares are reported in the financial statements as stock subscribed. However, the anticipated agreements have not yet been executed therefore the conditions that give rise to their issuance have not been satisfied. The Company does not consider these shares to be owned by the certificate holders.

The Company's transfer agent (First American Stock Transfer, Inc.) confirms a hold notification on the subject shares and that no transfers have been made or attempted with respect to these certificates.

On June 9, 2005 the company filed notice with the SEC of its intent to raise \$1,100,000 in a private placement to accredited investors wherein one share of common stock would be issued for every \$0.55 invested. As of 28 July 2005 2,000,000 common shares were issued and the \$1,100,000 was raised.

On July 29, 2005 the company filed notice with the SEC of its intent to raise \$935,000 in a private placement to accredited investors wherein one share of common stock would be issued for every \$0.55 invested. The company estimates completion of this raise by 6 August 2005.

In preparation for manufacturing its new technologies, the company has entered into an operating lease with the option to buy a 28,000 square foot light manufacturing facility. The effective date of the lease is August 15, 2005 with a monthly base payment of \$16,800. The building will house the assembly of its new tankless water heating products and will include 7,000 to 8,000 square feet of administrative offices.

## ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OR PLAN OF OPERATION.

The following Discussion and Analysis should be read in conjunction with the financial statements and notes included in this Form 10-QSB and the Company's annual report on Form 10-KSB for the year ended December 31, 2004.

(a)

### Plan of Operation.

Tankless Systems Worldwide, Inc., a Nevada corporation ( Tankless ), was originally organized on November 23, 1993 as Amexan, Inc.; the name was changed on June 1, 1998 to Nostalgia Motorcars, Inc. ( Nostalgia ), to Elution Technologies, Inc., on June 11, 2002, and changed again on June 4, 2003, to Tankless Systems Worldwide, Inc.

Tankless has three subsidiary corporations. On November 7, 2003, the Company acquired Envirotech Systems Worldwide, Inc. (Envirotech), a private Arizona corporation, as a wholly owned subsidiary. In January 2004, it formed ION Tankless, Inc.(ION), an Arizona corporation, to do research, development and marketing of new tankless heating technologies. In January 2005, it organized Valeo Industries, Inc. (Valeo), a Nevada corporation, to license ION technologies and to manufacture and distribute products using those technologies. Except as otherwise specified, all references herein to the "Company" refer to Tankless and its wholly-owned subsidiaries, Envirotech, ION and Valeo. The Company's fiscal year ends on December 31.

The Company is in the business of designing, developing, manufacturing and marketing several models of an electronic, tankless water heater. The water heater is small, easy to install and supplies endless amounts of hot water with energy savings. The unit is a microprocessor controlled electric water heater contained in a compact unit, eliminating the space demands of conventional water heaters. It incorporates automatic, precise temperature controls. It saves energy, space, and water and is suitable to all areas of the U.S. and worldwide.

On November 7, 2003, the Company acquired all of the issued and outstanding shares of Envirotech Systems Worldwide, Inc., a private Arizona corporation ( Envirotech ) in exchange for an equal number of shares of Common Stock of the Company (the Envirotech Agreement ). As of the close of business on November 7, 2003, Tankless issued 8,366,778 shares of its common stock, \$0.001 par value, in a one-for-one stock exchange. Subsequently, 2,075,000 of these shares were returned to Tankless by the former principal officers and directors of Envirotech and cancelled by Tankless. Envirotech is held and operated as a wholly-owned subsidiary of Tankless.

Envirotech was organized December 9, 1998 and has a limited history of operations. The initial period of its existence involved research and development of a line of electronic, tankless water heaters. The first sales of its products occurred in calendar year 2000. Audited financial statements for Envirotech at the date of acquisition, November 7, 2003, and the period then ending, indicate cumulative losses of \$4,043,572, \$489,658 of which is attributable to a repurchase of a distributorship in a major market where Envirotech believed the distributor was not performing well as the market would justify.

Proprietary rights to the design of the electronic tankless water heater were Envirotech's principal assets. Envirotech was granted a patent by the United States Patent and Trademark Office for its Modular Tankless Electronic Water Heater (ETWH) (Patent No. US 6,389,226 B1). A competitor, however, brought the value of that patent, into question with the filing of a patent infringement lawsuit. In 2002, Envirotech was named as a defendant in a patent infringement suit alleging that Envirotech's product infringed upon a patent owned by David Seitz and Microtherm, Inc. Mr. Seitz and Microtherm filed the suit in the United States District Court for the Southern District of Texas, Houston Division (the Houston suit). Management believed, and continues to believe, that the products manufactured and

distributed by Envirotech did not infringe on the patents of others and that it would prevail on the merits. However, Envirotech's counsel withdrew and due to a lack of funds, Envirotech was unable to obtain new counsel. The Court ordered Envirotech to appear with new counsel by August 9, 2004 or default would be entered against it. No contingency has been recorded with regard to this matter. At a hearing in May 2005, the Bankruptcy Court agreed that the plaintiff in the Houston suit could, if he so chose, re-open the case for the sole purpose of determining whether Envirotech is liable and, if so, to what extent. The Court, however, retained jurisdiction over the matter with respect to how such a liquidated claim would be treated in the Bankruptcy case.

In order to avoid an entry of default in the Houston suit, which would have found that Envirotech's product infringed upon the patents of the plaintiffs, and because several creditors not related to the supply of parts or the assembly of products had obtained judgments against Envirotech, on August 6, 2004, Envirotech filed for relief under Chapter 11 of the United States Bankruptcy Code in the United States Bankruptcy Court for the District of Arizona. The Houston suit and the other litigation arose out of decisions made and actions taken by Envirotech's management prior to its acquisition by Tankless.

As of the date of filing of the Chapter 11 Bankruptcy Petition, Envirotech had liabilities of approximately \$1.6 million. With the exception of a guarantee to one critical supplier in the amount of approximately \$42,500, Tankless has not assumed any liability for the obligations of Envirotech. The filing of the Bankruptcy Petition has stayed all creditors and suits. In December 2004 the Company filed a Plan of Reorganization, which initially failed to achieve the requisite approval of creditors. Subsequently, certain of the creditors have indicated they will vote to approve the Plan and a Confirmation Hearing is scheduled August 16, 2004, in the Bankruptcy Court. The Company expects that its Plan of Reorganization will be approved.

Although the Company believes that Plan of Reorganization will be accepted by the creditors and approved by the Court, Tankless has no way to assure that such will occur. Nonetheless, Tankless has concluded that the success of the Company is not contingent upon the survival of Envirotech. The filing of the bankruptcy petition by Envirotech did not adversely affect the ongoing operations of the Company or its research and development subsidiary, ION Tankless, Inc. However, because of the patent infringement challenge and other uncertainties associated with its Bankruptcy, Envirotech has discontinued marketing of all models of the ESI-2000 tankless water heater previously manufactured by it.

In January 2004, Tankless formed a wholly-owned, non-operating subsidiary, ION Tankless, Inc., through which it has since conducted research and development on alternative heating technologies and products. Tankless has invested heavily in a concerted R & D program to develop new and innovative methods of heating water which has resulted in the filing of applications for several patents involving dozens of claims for inventions. As a result of a year-long research and development program, new products have been developed and are ready for licensing and production. This technology is considered state of the art and is expected to set the standard for the future of the tankless water heater industry. ION holds all patents and intellectual property of the Company arising out of this research and development program and expects to license such property to an affiliated entity for manufacturing and distribution.

Valeo was organized by Tankless in January 2005 as a wholly-owned operating subsidiary. Valeo will license technology from ION and manufacture, market and distribute several lines of water heating products. Valeo will soon begin production and distribution of two new product lines that incorporate innovative technology not previously used in the water heating market. These new products, based on proprietary technology, are expected to serve as the foundation for the future growth of the Company.

During 2004, the Company sold \$1,075,000 principal amount of 10% senior notes due one year from date of issue and 537,500 shares of common stock in private placements. We used the net proceeds from the offerings to pursue research and development of new products; proceed with marketing,

manufacturing and sales of existing products through Envirotech; hire additional personnel and engage consultants as needed; and for general working capital purposes. Between December 31, 2004 and June 30, 2005 the Company issued 774,201 common shares for services valued at \$184,701, 540,909 common shares for \$297,500 cash, and 312,626 shares in satisfaction of total principal and interest on notes payable in the amount of \$171,945. The proceeds from the sales of stock were used to continue research and development, to extinguish certain short-term indebtedness, to acquire tools and dies and raw materials inventory for planned operations, engage consultants as needed, and for general operating purposes.

As of August 12, 2005, the business office of the Company was located at 7650 E. Evans Rd., Suite C, Scottsdale, Arizona 85260. Envirotech leases these offices pursuant to an amended lease agreement that expires on June 30, 2006. However, the Company may terminate the lease on 120 days notice. Prior to removal of the offices of the Company to the above location, the Company occupied space at 2920 E. Camelback Rd., Suite 150, Phoenix, Arizona 85016. These offices were leased by an unrelated party, subleased to Messrs. Thomas and David Kreitzer and made available by them to the Company on a month-by-month basis at no cost.

The Company has recently contracted to purchase an approximately 28,000 square foot light industrial building in Chandler, Arizona. The agreement provides that the Company will occupy the building on a triple-net lease basis until close of escrow. The monthly base rent is approximately \$17,000 and the Company expects to occupy the building on August 15, 2005. From this facility the Company plans to manufacture, market and distribute a new line of water heating products beginning in the fourth quarter of this year.

The Company's fiscal year ends on December 31. At June 30, 2005, Tankless had two part time employees (Thomas Kreitzer and David Kreitzer) both of whom served at nominal compensation and Valeo, its subsidiary, had four full-time employees. The Company anticipates adding several full time employees in the near future in management and for administrative and technical support.

Tankless currently has 15,037,238 shares issued and outstanding. The shares of common stock of Tankless are traded on the National Association of Securities Dealers (NASD) Over-the-Counter Bulletin Board (OTCBB) under the ticker symbol TSYW.

The foregoing Plan of Operation may contain "forward looking statements" within the meaning of Rule 175 under the Securities Act of 1933, as amended, and Rule 3b-6 under the Securities Act of 1934, as amended, including statements regarding, among other items, the Company's business strategies, continued growth in the Company's markets, projections, and anticipated trends in the Company's business and the industry in which it operates. The words "believe," "expect," "anticipate," "intends," "forecast," "project," and similar expressions identify forward-looking statements. These forward-looking statements are based largely on the Company's expectations and are subject to a number of risks and uncertainties, certain of which are beyond the Company's control. The Company cautions that these statements are further qualified by important factors that could cause actual results to differ materially from those in the forward looking statements, including, among others, the following: reduced or lack of increase in demand for the Company's products, competitive pricing pressures and the level of expenses incurred in the Company's operations. In light of these risks and uncertainties, there can be no assurance that the forward-looking information contained herein will in fact transpire or prove to be accurate. The Company disclaims any intent or

obligation to update "forward looking statements."

(b) Liquidity and Capital Resources

As of June 30, 2005 the Company had established source of revenue from sales of water heater units. Nonetheless, it has a negative working capital of \$2,788,567 and has accumulated losses of \$4,120,144.



Without realization of additional capital, it would be unlikely for the Company to continue as a going concern.

### ITEM 3. CONTROLS AND PROCEDURES

Our Chief Executive Officer and Principal Accounting Officer (the Certifying Officer ) is responsible for establishing and maintaining disclosure controls and procedures for the Company. The Certifying Officer has designed such disclosure controls and procedures to ensure that material information is made known to him, particularly during the period in which this report was prepared. The Certifying Officer has evaluated the effectiveness of the Company's disclosure controls and procedures as of the end of the period covered by this report and believes that the Company's disclosure controls and procedures are effective based on the required evaluation. During the period covered by this report, there were no changes in internal controls that materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

PART II

ITEM 1. LEGAL PROCEEDINGS

The Company is a defendant in a lawsuit filed by a law firm that formerly represented the Company. The suit claims legal fees owed in the amount of approximately \$7,500. The Company disputes this claim and expects to prevail in the matter.

Envirotech Systems Worldwide, Inc. ( Envirotech ), is a wholly-owned subsidiary of the Company. Prior to the acquisition of Envirotech by Tankless, Envirotech was the defendant in a lawsuit filed by a former distributor alleging a breach of a Distributor Agreement entered into with Envirotech in May 1998. On August 13, 2003, Envirotech entered into a Settlement Agreement and Release pursuant to which Envirotech agreed to pay the distributor the sum of \$520,500 in installments over a period of ten years. The obligations under this Settlement Agreement are secured by a Security Agreement covering all assets of Envirotech except its intellectual properties, as defined therein, subordinated, however, to a first lien on such assets granted to the law firm of Jennings, Strouss & Salmon in 2001 and 2002 by Envirotech to secure two promissory notes given in satisfaction of legal fees. As part of the settlement, Envirotech granted the distributor a Stipulated Judgment that was not to be filed of record so long as no default existed. On April 14, 2004, the distributor claimed a breach and filed the Stipulated Judgment. Management believes no default existed to warrant the filing of the judgment. Nonetheless, the filing of that judgment was a material consideration to the filing of the Chapter 11 Bankruptcy Petition discussed below.

Envirotech is also the defendant in a suit filed in 2002 in the U.S. District Court, for the Southern District of Texas, Houston, Texas (Civil Action No. H-02-4782, David Seitz and Microtherm, Inc., vs. Envirotech Systems Worldwide, Inc., and Envirotech of Texas, Inc. The Company is not affiliated with Envirotech of Texas, Inc. The suit alleges that Envirotech has infringed on the patent rights of others and seeks damages and an order to cease and desist. Envirotech engaged legal counsel to represent it in this matter. Management believes the suit is without merit and that Envirotech will prevail in the matter. In 2004 Envirotech's counsel withdrew and due to a lack of funds, Envirotech was unable to obtain new counsel. The Court ordered Envirotech to appear with new counsel by August 9, 2004 or default would be entered against it. In order to avoid an entry of default, which would have found, without a finding based on the merits, that Envirotech's product infringed upon the patent of Mr. Seitz and Microtherm, Envirotech filed for relief under Chapter 11 of the United States Bankruptcy Code in the United States Bankruptcy Court for the District of Arizona, on August 6, 2004 (discussed below). The obligations of Envirotech in this matter remain the sole liability of Envirotech and the parent company, Tankless, has not assumed any portion of such obligations. The filing of the petition with the Bankruptcy Court stayed all existing litigation, judgments and efforts to collect on judgments entered against Envirotech. At a hearing in May 2005, the Bankruptcy Court agreed that the plaintiff in the Houston suit could, if he so chose, re-open the Houston Case for the sole purpose of determining whether Envirotech is liable and, if so, to what extent. The Court, however, retained jurisdiction over the matter with respect to how such a liquidated claim would be treated in the Bankruptcy case.

In 2004 Envirotech was named in three separate lawsuits for unpaid legal and consulting fees totaling \$268,000. Envirotech believed it had meritorious defenses to each of these suits. On April 14, 2004, Envirotech settled one of these suits, considering it a nuisance claim. In connection with that settlement, Envirotech reimbursed the plaintiff for alleged out-of-pocket expenses and the Company issued 10,000 shares of common stock, restricted under Rule 144, to the plaintiff on the basis of a loan from the Company to Envirotech. In the other two suits Envirotech elected not to spend funds to defend the action and judgments were granted in the aggregate amount of approximately \$155,500. These judgments have been stayed through Bankruptcy Petition.

On August 6, 2004, Envirotech filed a Voluntary Petition for protection under Chapter 11 of the United States Bankruptcy Code in Phoenix, Arizona. The filing of this Petition with the Bankruptcy

Court has stayed all existing litigation, judgments and efforts to collect on the judgments. Envirotech was acquired by the Company in November 2003 in a stock-for-stock transaction and has been held and operated by the Company as an operating subsidiary. With the exception of a guarantee to one critical supplier in the current amount of approximately \$42,500, the Company has not assumed any liability for the obligations of Envirotech. As of the date of the filing of the Chapter 11 Bankruptcy Petition, Envirotech had liabilities of approximately \$1.6 million. Several creditors, not related to the supply of parts or the assembly of products, have obtained judgments against Envirotech and an action was pending in the U.S. District Court, Southern District of Texas, alleging patent infringement. All claims of creditors, including the above-mentioned judgments, and efforts to collect same, together with the litigation pending in the U.S. District Court in Houston, have been stayed during the pendency of the Bankruptcy proceedings. Envirotech filed a Plan of Reorganization and Disclosure Statement in December 2004, which initially failed to receive the requisite approval of its creditors. Subsequently, certain of the creditors have indicated they will vote to approve the Plan and a Confirmation Hearing is scheduled August 16, 2004, in the Bankruptcy Court. The Company expects that its Plan of Reorganization will be approved.

On August 13, 2004, Tankless filed a verified complaint in the United States District Court in and for the District of Arizona against three former officers, directors and principal shareholders of Envirotech, and Ronald Jay Edwin, a/k/a Ryan Edelstein, and others. The suit alleged, against various defendants, Breach of Fiduciary Duty, Aiding and Abetting Breach of Fiduciary Duty, Breach of Contract, Breach of Implied Covenant of Good Faith and Fair Dealing, Fraud and Intentional Misrepresentation, Conspiracy to Defraud, Arizona Securities Fraud, Federal Securities Fraud, Negligent Misrepresentation, Misappropriation of Trade Secrets and Confidential Business Information, Conversion/Embezzlement, Intentional Interference with Business Relations and Prospective Economic Advantage, Unjust Enrichment, and Promissory Estoppel. The Company sought various forms of relief including, but not limited to, Damages, Constructive Trust, Rescission and Injunctive Relief. A copy of this Complaint is available upon request made to the Company. Subsequently, the suit was voluntarily dismissed by the Company to facilitate settlement negotiations with each of the defendant parties. A settlement has been signed with Ronald J. Edwin the terms of which include, among other things, a permanent injunction against Mr. Edwin for the actions alleged. Settlements with each of the remaining defendants were achieved in the fourth quarter of 2004, resulting in the return and cancellation of 2,075,000 shares of common stock of the Company that had been issued in connection with the acquisition of Envirotech. In addition, all three defendants entered into non-compete agreements with the Company and agreed to various other terms sought by the Company. In connection with one of the settlements where the defendant returned a substantial block of his shares, the defendant was granted an option by the Company to acquire up to 100,000 shares of common stock at a price of \$0.55, for a period of one year. The option expires December 31, 2005.

Except as noted above, to the best knowledge of the officers and directors of the Company, neither the Company nor its subsidiaries, nor any of their respective officers or directors is a party to any material legal proceeding or litigation.

## ITEM 2. CHANGES IN SECURITIES

None

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

(a) During the year ended December 31, 2000, the Company issued five convertible notes payable, totaling \$100,000, which matured in March 2001. These notes bear interest at the rate of 12.5% per annum. Each note is subject to automatic conversion at the maturity date. As of the date of this filing, the notes have not yet been converted and are in default.

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

None

ITEM 5. OTHER INFORMATION

None

ITEM 6. EXHIBITS

(a)

Exhibits

31.1

Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

32.1

Certification Pursuant to U.S.C. 18 Section 1350

SIGNATURES

In accordance with Section 13 of the Exchange Act, the Company has caused this report to be signed on its behalf by the undersigned, hereunto duly authorized

TANKLESS SYSTEMS WORLDWIDE, INC.

(formerly Elution Technologies, Inc.)

Date: August 15, 2005

By: /s/ Thomas Kreitzer

Thomas Kreitzer,

Chief Executive Officer

and Principal Accounting Officer