

**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

FORM 10-QSB

(Mark One)

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

For the quarterly period ended September 30, 2004

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

For the transition period from _____ to _____

333-64122

(Commission file number)

VERDISYS, INC.

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

California

(State or other jurisdiction of incorporation or organization)

22-3755993

(IRS Employer Identification No.)

14550 Torrey Chase Blvd.,

Houston, Texas 77014

(Address of principal executive offices)

(281) 453-2888

(Issuer's telephone number)

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

Check whether the issuer (1) filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act during the past 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

The number of shares outstanding of each of the issuer's classes of common equity as of November 8, 2004: 32,999,505 shares of common stock.

The common stock of Verdisys, Inc. is traded over-the-counter on the OTC Bulletin Board under the symbol "VDYS.OB".

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

[Table of Contents](#)

Verdisys, Inc.

Index

	<u>Page Number</u>
PART I. FINANCIAL INFORMATION	
Item 1. Financial Statements	3
Item 2. Management’s Discussion and Analysis of Financial Condition and Plan of Operations	11
Item 3. Controls and Procedures	14
Part II. OTHER INFORMATION	
Item 1. Legal Proceedings	14
Item 2. Change in Securities and Use of Proceeds	14
Item 3. Defaults Upon Senior Securities	14
Item 4. Submission of Matters to a Vote of Security Holders	14
Item 5. Other Information	14
Item 6. Exhibits and Reports on Form 8-K	14
SIGNATURES	16

[Table of Contents](#)

VERDISYS, INC.

PART I. FINANCIAL INFORMATION

ITEM 1. Financial Statements

	Page Number
Balance Sheet as of September 30, 2004	4
Statements of Operations, for the three and nine months ended September 30, 2004 and 2003	5
Statements of Cash Flow, for the nine months ended September 30, 2004 and 2003	6
Notes to Financial Statements	7

VERDISYS, INC.

BALANCE SHEET
September 30, 2004

ASSETS	
Current Assets	
Cash	\$ 122,764
Accounts receivable, net of allowance for doubtful accounts of \$100,000	65,198
Accounts receivable from related parties	20,547
Prepaid expenses	56,965
Total Current Assets	265,474
Property and equipment, net of accumulated depreciation of \$146,883	643,601
License, net of accumulated amortization of \$460,828	4,564,172
Total Assets	\$ 5,473,247
LIABILITIES AND STOCKHOLDERS' DEFICIT	
Current Liabilities	
Accounts payable	\$ 581,782
Accrued expenses	777,391
Deferred revenue	881,127
Guarantee of third party debt	300,000
Customer deposit	275,000
Convertible notes payable, net of unamortized discount of \$86,290	313,710
Notes payable to related parties, net of unamortized discount of \$21,770	163,229
Total Current Liabilities	3,292,239
Long Term Liabilities Deferred revenue, less current portion	52,975
Total Liabilities	3,345,214
Commitments & Contingencies	
Stockholders' Equity	
Convertible preferred stock, no par value, 40,000,000 shares authorized	
Series A, none issued and outstanding	—
Series B, none issued and outstanding	—
Common stock, \$.001 par value, 50,000,000 shares authorized, 31,721,727 shares issued and outstanding	31,722
Additional paid in capital	24,739,033
Accumulated deficit	(22,642,722)
Total Stockholders' Equity	2,128,033
Total Liabilities and Stockholders' Equity	\$ 5,473,247

VERDISYS, INC.

STATEMENTS OF OPERATIONS
Three and Nine Months Ended September 30, 2004 and 2003

	Three Months		Nine Months	
	2004	2003	2004	2003
Revenue				
Satellite Services Third parties	\$ 154,906	\$ 27,824	\$ 401,705	\$ 362,115
Drilling Services Third parties	427,519	—	694,180	—
Total revenue	582,425	27,824	1,095,885	362,115
Cost of services Provided				
Satellite Services Third parties	153,668	786,021	464,874	1,176,085
Drilling Services Third parties	272,080	—	688,906	—
Total Cost of Services Provided	425,748	786,021	1,153,780	1,176,085
Gross Margin (loss)	156,677	(758,197)	(57,895)	(813,970)
Selling, general & administrative	936,591	770,119	3,382,053	3,948,498
Depreciation & amortization	130,051	62,078	395,982	108,792
Bad debts	50,000	19,999	50,000	19,999
Debt forgiveness Income	—	—	—	(460,235)
Total operating expenses	1,116,642	852,196	3,828,035	3,617,054
Operating loss	(959,965)	(1,610,393)	(3,885,930)	(4,431,024)
Other expense				
Interest income	31	—	48	—
Interest expense	(14,544)	(43,167)	(454,422)	(140,006)
Loss on sale of equipment	(1,900)	—	(1,900)	—
NET LOSS	\$ (976,378)	\$ (1,653,560)	\$ (4,342,204)	\$ (4,571,030)
Basic and diluted net loss per share	\$ (.03)	\$ (.06)	\$ (.14)	\$ (.21)
Weighted average shares outstanding	31,523,265	26,783,077	30,986,520	21,491,391

[Table of Contents](#)

VERDISYS, INC.
STATEMENTS OF CASH FLOW
Nine Months Ended September 30, 2004 and 2003

	<u>2004</u>	<u>2003</u>
Cash Flows From Operating Activities		
Net loss	\$(4,342,204)	\$(4,571,030)
Adjustments to reconcile net loss to net cash used in operating activities:		
Stock issued for services	948,192	1,326,329
Issuance of options and warrants for services	290,844	1,861,622
Depreciation and amortization	390,089	108,792
Loss on sales of equipment	1,900	—
Amortization of discount on notes payable	25,685	—
Debt forgiveness income	—	(460,235)
Bad debt	50,000	19,999
Changes in:		
Accounts receivable	24,947	(88,833)
Accounts receivable – related party	3,413	42,620
Other current assets	—	(25,468)
Accounts payable	261,095	(302,674)
Accrued expenses	281,540	261,353
Customer deposit	206,718	60,000
Deferred revenue	72,906	611,681
Net Cash Used In Operating Activities	<u>(1,784,875)</u>	<u>(1,155,844)</u>
Cash Flows From Investing Activities		
Purchase of property and equipment	(3,705)	(369,701)
Cash payments for license	—	(100,000)
Proceeds from the sale of equipment	12,500	—
Net Cash Used In Investing Activities	<u>8,795</u>	<u>(469,701)</u>
Cash Flows From Financing Activities		
Proceeds from sales of common stock	359,000	1,982,150
Proceeds from exercise of warrants	81,217	329,251
Proceeds from notes payable to related parties	220,000	50,000
Payments on notes payable to related parties	(35,000)	(155,894)
Proceeds from convertible notes	400,000	—
Payments on note payable on license	(500,000)	(379,596)
Net Cash Provided by Financing Activities	<u>525,217</u>	<u>1,825,911</u>
Net change in cash	<u>(1,250,863)</u>	<u>200,366</u>
Cash at beginning of period	1,373,627	135
Cash at end of period	<u>\$ 122,764</u>	<u>\$ 200,501</u>
NON-CASH:		
Stock issued for notes payable license	\$ 1,184,808	\$ —
Discount on notes payable	133,746	—

VERDISYS, INC.
NOTES TO FINANCIAL STATEMENTS

NOTE 1 - BASIS OF PRESENTATION

The accompanying, unaudited interim financial statements of Verdisys, Inc. ("Verdisys") have been prepared in accordance with accounting principles generally accepted in the United States of America and the rules of the Securities and Exchange Commission ("SEC"), and should be read in conjunction with the audited financial statements and notes thereto contained in Verdisys' Annual Report filed with the SEC on Form 10-KSB. In the opinion of management, all adjustments, consisting of normal recurring adjustments, necessary for a fair presentation of financial position and the results of operations for the interim periods presented have been reflected herein. The results of operations for the interim periods are not necessarily indicative of the results to be expected for the full year. Notes to the financial statements which would substantially duplicate the disclosure contained in the audited financial statements for 2003 as reported in the 10-KSB have been omitted.

Revenue recognition. Revenue is recognized on well drilling operations when persuasive evidence of an arrangement exists, the lateral drilling is complete, the price is fixed or determinable and collectibility is reasonably assured.

NOTE 2 – STOCK OPTIONS AND WARRANTS

Stock options and warrants. Verdisys accounts for non-cash stock-based compensation issued to non-employees in accordance with the provisions of SFAS No. 123 and EITF No. 96-18, Accounting for Equity Investments That Are Issued to Non-Employees for Acquiring, or in Conjunction with Selling Goods or Services. Common stock issued to non-employees and consultants is based upon the value of the services received or the quoted market price, whichever value is more readily determinable. Verdisys accounts for stock options and warrants issued to employees under the intrinsic value method. Under this method, Verdisys recognizes no compensation expense for stock options or warrants granted when the number of underlying shares is known and the exercise price of the option or warrant is greater than or equal to the fair market value of the stock on the date of grant.

During the first quarter of 2004, Verdisys granted 310,000 ten year options to officers and non-employee directors with exercise prices at the then market price of \$4.28. The options to officers vest monthly over 12 months and the options to non-employee directors' vest immediately.

During the second quarter of 2004, Verdisys granted 72,000 options to non-employee directors with an exercise price of \$2.20. The options vest immediately.

During the third quarter of 2004, Verdisys granted 140,000 ten year warrants to employees with an exercise price of \$.10 and 770,000 ten year options to employees with an exercise price of \$.90. The options vest quarterly over 4 years and the warrants vest immediately.

[Table of Contents](#)

The following table illustrates the effect on net loss and net loss per share if Verdisys had applied the fair value provisions of FASB Statement No. 123, *Accounting for Stock-Based Compensation*, to stock-based employee compensation.

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2004	2003	2004	2003
Net loss as reported	\$ (976,378)	\$(1,653,560)	\$(4,342,204)	\$(4,571,030)
Add: stock based compensation determined under intrinsic value-based method	39,698	—	290,844	—
Less: stock based compensation determined under fair value-based method	(89,474)	(299,008)	(1,001,619)	(299,008)
Pro forma net loss	<u>\$(1,026,154)</u>	<u>\$(1,952,568)</u>	<u>\$(5,052,979)</u>	<u>\$(4,870,038)</u>
Basic and diluted net loss per common share:				
As reported	\$ (.03)	\$ (.06)	\$ (.14)	\$ (.21)
Pro forma	(.03)	(.07)	(.16)	(.23)

The weighted average fair value of the stock options granted during 2004 and 2003 was \$1.19 and \$.50, respectively. Variables used in the Black-Scholes option-pricing model include (1) 2.0% risk-free interest rate, (2) expected option life is the actual remaining life of the options as of each year end, (3) expected volatility is zero, and (4) zero expected dividends.

NOTE 3 – LATERAL DRILLING LICENSE & NOTE PAYABLE ON LICENSE TO RELATED PARTY

Verdisys did not make the December 2003 or January 2004 payment on the note payable. In February 2004, Verdisys and the licensor agreed to restructure the note payments. Verdisys agreed to issue the licensor 300,000 shares of common stock, \$100,000 cash and a note payable for \$400,000 due on May 15, 2004 for the unpaid amounts due under the original note. The 300,000 shares had a value of \$1,920,000 with \$1,184,808 reducing the overall note balance and \$735,192 recognized as compensation expense. On May 14, 2004 Verdisys paid the final installment on the Note.

NOTE 4 – CUSTOMER DEPOSITS

In May 2004, Verdisys agreed to a second contract to drill laterals for Maxim Energy (“Maxim”), a company controlled by Verdisys’ former CEO, Dan Williams. Verdisys has stipulated that all services to Maxim will be paid for in advance. As of September 30, 2004, Maxim had paid Verdisys \$270,000 and El Paso Energy had paid \$5,000 for services yet to be rendered.

NOTE 5 – DEFERRED REVENUE

Satellite bandwidth contracts cover a period between 12 and 36 months. In select engagements, Verdisys receives cash in advance and recognizes revenue evenly over the contract. Deferred revenue related to satellite services totaled \$368,351. \$315,376 will be recognized in the year ended September 30, 2005 and \$52,975 will be recognized during the years subsequent to September 30, 2005.

Verdisys also deferred revenue collected for lateral drilling service contracts. In June 2003, Verdisys signed an agreement to drill wells for Edge Capital (“Edge”). Edge, through a third party financing source, paid Verdisys \$497,000 in 2003. Verdisys has inadequate documentation to substantiate what services were actually performed, and Edge is disputing whether the services were performed at all. Management is attempting to substantiate what services were actually performed and continues to gather evidence to substantiate the services. As of September 30, 2004, the \$497,000 is included in deferred revenue.

In 2003 Verdisys billed \$666,250 to Energy 2000 for services performed in 2003. Verdisys received \$397,500. However, Verdisys has inadequate documentation to substantiate whether some of the services were performed. Verdisys was able to substantiate \$328,750 of revenue leaving \$68,750 in deferred revenue.

NOTE 6 – NOTES PAYABLE

During the third quarter, Verdisys issued \$350,000 in Convertible Notes to third party lenders, carrying an 8% interest rate and 175,000 shares in warrants at an exercise price of \$0.001. Verdisys has an option to convert the shares at \$2 per share when they have traded above that level for more than 20 trading days. The notes were discounted by the relative fair value of the warrants which totaled \$98,589. \$12,299 of the discount was expensed through September 30, 2004.

[Table of Contents](#)

NOTE 7 – NOTES PAYABLE TO RELATED PARTIES

During the second and third quarter of 2004, officers and directors of Verdisys loaned Verdisys \$185,000. The notes mature in 12 months, carry interest of 8% and have one year warrants attached with an exercise price of \$2.00. The notes were discounted by the relative fair value of the warrants which totaled \$35,157. \$13,387 of the discount was expensed through September 30, 2004.

Verdisys also borrowed \$35,000 from a director, which loan was repaid by Verdisys within a month.

NOTE 8 – STOCKHOLDERS EQUITY

During the first quarter of 2004, Verdisys issued 409,935 shares of common stock pursuant to stock option exercises for total consideration of \$40,993.

In February 2004, Verdisys issued 395,022 shares of common stock pursuant to the cashless exercise of a warrant for 400,000 shares of common stock at a price of \$0.10 per share.

In March 2004, Verdisys issued 300,000 shares of common stock to Carl Landers in connection with the renegotiation of the note payable to Mr. Landers for the licensing of his lateral drilling technology. See note 3 for details.

During the second quarter of 2004, Verdisys issued 402,241 shares of common stock pursuant to stock option exercises for total consideration of \$40,224.

During the second quarter of 2004, Verdisys sold 179,500 shares of common with 71,800 warrants attached for total consideration of \$359,000. The warrants were valued at \$86,207 and the stock was valued at \$272,793.

During the third quarter of 2004, Verdisys issued 47,950 shares of common stock for fundraising commissions and another 300,000 shares of common stock for a lawsuit settlement valued at \$213,000.

NOTE 9 – LITIGATION

Except as set forth below, there have been no material developments in Litigation other than as reported in the Company's Annual Report on Form 10K-SB.

As previously disclosed, Verdisys initiated a lawsuit against Edge Capital that requests a declaratory judgment that a purported agreement between Verdisys and Edge is not enforceable. It was filed in Montgomery County, Texas in February 2004. The lawsuit arises from Edge's contention that one of Verdisys' ex-officers committed Verdisys to purchase certain alleged oil and gas properties from Edge. Edge filed a counterclaim against Verdisys and asserts claims against Dan Williams (Verdisys' former President and CEO), Eric McAfee (Verdisys' former Vice Chairman), Ron Robinson, Frederick Ruiz, Joseph Penbera, James Woodward, John Block, and Andrew Wilson. Edge has also made claims against Solarcom, L.L.C., DeLage Landen Financial Services, Inc., and Allen Voight. Edge seeks to enforce the agreement Verdisys challenges, and alleges several causes of action including claims for fraud, breach of contract, negligence, and conspiracy. Edge has asserted that it has sustained actual damages in excess of \$85 million, and has claimed punitive damages as well. Verdisys believes it has meritorious and complete

[Table of Contents](#)

defenses to the claims asserted in the lawsuit and intends to vigorously defend itself. If Edge prevails, it may obtain significant damages that may have a material adverse effect on Verdisys' financial condition.

Edge and one of its apparent owners, Frazier Ltd., initiated a lawsuit in Summit County, Ohio against Solarcom, L.L.C., DeLage Landen Financial Services, Inc., Verdisys, Inc., and Firstmerit Bank, N.A. that sought an injunction against the draw against a letter of credit pledged as collateral for a credit advanced to Edge. Edge asserted that its transaction with Verdisys was the product of fraud and that its creditor, DeLage Landen as assignee from Solarcom, should not be allowed to draw against Edge's letter of credit from Firstmerit. The Ohio state court denied Edge's request for a temporary injunction. The pleadings in the Ohio action do not include any claim for damages from Verdisys and Verdisys is unable to determine whether an adverse judgment would have a material adverse effect on Verdisys' financial condition.

In September, Verdisys settled the claim by Scooter's Convenience by issuing 300,000 shares of Verdisys to Scooters in a private transaction. In connection with the settlement, the Company agreed to register the resale of the shares issued to Scooter's with the SEC. See note 7 for details.

In connection with its financing in October 2003 with Gryphon Master Fund, L.P, Verdisys agreed to provide certain registration rights to the investors. As part of the registration rights agreement with Gryphon, Verdisys agreed to register the shares on or before March 2004. In the event that Verdisys failed to comply with the required deadlines, Verdisys could be subject to certain liquidated damages. Gryphon has made a claim against Verdisys for the maximum liquidated damages in an amount of \$400,000. Verdisys was notified that legal action has been filed against Verdisys by Gryphon Master Fund, L.P. for the liquidated damages as well as its entire investment in Verdisys for a total of \$6,200,000, together with attorney's fees and punitive damages. The parties are currently engaged in discovery. The Company intends to vigorously defend itself in this matter. If Gryphon prevails, however, this may have a material adverse effect on the Company's financial condition.

In July, 2004 Verdisys was informed that a former CEO of Verdisys filed a lawsuit against Verdisys for breach of contract and wrongful discharge. These claims seek relief in excess of \$500,000 related to an alleged employment agreement and also seek damages related to an excess of 4,000,000 stock options claimed pursuant to the alleged agreement. The company has only recently received notice of these claims. The lawsuit was filed in state court in San Diego, California. Verdisys intends to vigorously defend itself.

NOTE 10 – SETTLEMENT OF ACCOUNTS PAYABLE

In the third quarter of 2004, Verdisys leased one of its Lateral Drilling Units to Advanced Hydraulic Manufacturing in exchange for the forgiveness of \$97,720 in accounts payable. This was recognized as an increase in rental revenue and a decrease in accounts payable.

NOTE 11 – SUBSEQUENT EVENTS

Energy 2000

In October, 2004 Verdisys entered into an agreement with Berg McAfee Companies, Energy 2000 NGC, Inc. (Energy 2000), and Eric McAfee to settle several outstanding legal issues. Energy 2000 has agreed to settle a Finders Fee and Lateral Drilling services dispute by delivering 300,000 shares of Natural Gas Systems stock into escrow for Verdisys. The Company plans to have these shares monetized as soon as practical. Furthermore, to settle a contemplated third party legal dispute, Verdisys and the parties have exchanged 500,000 shares of Natural Gas Systems stock for 500,000 of Verdisys shares and Verdisys has delivered into escrow an additional 250,000 shares. Verdisys also has agreed to dismiss the Quikview, Inc. lawsuit, which it had filed against certain individuals. Lastly, Berg McAfee Companies and Eric McAfee have loaned Verdisys \$200,000 under the same terms and conditions, with the exception of maturity dates, as the Convertible Notes issued in the third quarter described above.

Item 2. Management's Discussion and Analysis of Financial Condition and Plan of Operations

Forward-Looking Statements

This statement may include projections of future results and "forward looking statements" as that term is defined in Section 27A of the Securities Act of 1933 as amended (the "Securities Act"), and Section 21E of the Securities Exchange Act of 1934 as amended (the "Exchange Act"). All statements that are included in this Quarterly Report, other than statements of historical fact, are forward looking statements. Although management believes that the expectations reflected in these forward looking statements are reasonable, it can give no assurance that such expectations will prove to have been correct. Any statements made in this filing other than those of historical fact, about an action, event or development, are forward looking statements. The forward looking statements in this filing involve known and unknown risks and uncertainties, which may cause Verdisys' actual results in future periods to be materially different from any future performance that may be suggested in this release. Such factors may include risk factors including but not limited to: changes in technology, reservoir or sub-surface conditions, the introduction of new services, commercial acceptance and viability of new services, fluctuations in customer demand and commitments, pricing and competition, reliance upon subcontractors, the ability of Verdisys' customers to pay for our services, together with such other risk factors as may be included in the Company's periodic filings on Form 10-KSB, 10-QSB, and other current reports.

Financial Summary

Three Months Ended September 30, 2004 Compared to Three Months Ended September 30, 2003

Verdisys incurred \$582,425 in revenues and a net loss of \$976,378 for the quarter ended September 30, 2004 as compared to revenues of \$27,824 and net loss of \$1,653,560 for the quarter ended September 30, 2003. Revenues increased as a result of an increase in lateral drilling and satellite services activity for the quarter. There were no comparable lateral drilling revenues in 2003. The Net Loss decreased as a result of higher gross margins associated with the increased revenues, which were partially offset by higher selling, general and administration expenses ("SG&A") associated with an increase in non-cash stock, and warrant expense associated with the issuance of debt and settlement of a certain lawsuit.

Revenues

Lateral Drilling Services

Lateral Drilling Services' revenues were \$427,519 and \$0 for the three months ended September 30, 2004 and three months ended September 30, 2003, respectively. The increase in revenues for the quarter was primarily associated with revenues from the commencement of a contract with the Department of Energy, work performed for Maxim Energy and the rental of a rig to Advanced Hydraulics. The Company did not have a Lateral Drilling business in the quarter ended September 30, 2003.

As noted in the Subsequent Events section, effective as of October 27, 2004, Verdisys has entered into a Licensing Agreement to develop a new generation of lateral drilling technology. In the short term, the development activity will decrease lateral drilling revenues until such time as the Landers equipment is retrofitted and the new technology rigs are commissioned.

Satellite Communications Services

Satellite Communication Services' revenues for the quarter ended September 30, 2004 were \$154,906 compared to the quarter ended September 30, 2003 of \$27,824. Revenue increased in the quarter due to higher hardware sales of satellite equipment to Exxon/Mobil and Kellogg, Brown and Root and increased satellite bandwidth associated with the services to Noble Energy, Texas A&M, Dynegy and Kellogg, Brown and Root which were not in service in the prior year. As hardware is sold, Verdisys recognizes the revenue in the period it is delivered to the customer. The associated bandwidth revenue is amortized over the period benefited. Cash collected for bandwidth is recorded as deferred revenue. At September 30, 2004 there was \$368,351 reflected on the balance sheet as deferred revenue relating to Satellite Communications.

[Table of Contents](#)

Net Loss

The Net Loss decreased as a result of higher gross margins associated with the increased revenues, which was partially offset by higher SG&A expense associated with an increase in non-cash stock, and warrant expense associated with the issuance of debt and settlement of a certain lawsuit.

Nine Months Ended September 30, 2004 Compared to Nine Months Ended September 30, 2003

Net Loss

The Net Loss for the nine months ended September 30, 2004 decreased primarily as a result of higher revenues and greater margin contribution compared to the prior year, offset by liquidated damages resulting from the failure to file a timely registration statement and non-cash compensation expense associated with the renegotiation of the Landers note payable partially offset by the absence of debt forgiveness income in 2004.

Liquidity and Capital Resources

Capital Expenditures

For the three and nine month periods ended September 30, 2004, capital expenditures excluding capitalized interest, were \$3,705 and \$3,705, respectively, as compared to \$369,701 and \$369,701 for the comparable periods in 2003.

Liquidity

As of September 30, 2004 the Company's cash balance was \$122,764. As noted in the Independent Auditors Report (See Financial Note 2 to the December 31, 2003 Financial Statements) due to the continued substantial operating losses that the Company has incurred raises substantial doubt as to the Company's ability to continue as a going concern. The Company is in an early stage of development and is rapidly depleting its cash resources, therefore it has determined that it will need to raise additional financing in the short term to continue in operation and fund future growth. The Company has also incurred liquidated damages up to a cap of \$400,000 related to the timing of providing registration rights for the private financing that it arranged in November 2003. If we are unable to finance the liquidated damages, this would have a material adverse effect on the Company. The Company is also subject to significant contingent liabilities as more fully described in the Notes to the Financial Statements. See Note 8, Litigation.

The Company currently plans to raise additional financing in the quarter ending December 31, 2004. The use of stock for currency in financing or making acquisitions may be heavily curtailed while the Company is under SEC investigation. (See Financial Note 16 to the December 31, 2003 Financial Statements) If we are unable to arrange new financing or generate sufficient revenue from new business arrangements, the Company will be unable to continue in its current form and will be forced to restructure or seek creditor protection.

As noted in the Subsequent Events section, Verdisys has entered into an agreement to accept 300,000 shares of common stock of Natural Gas Systems, Inc. (the "NGS Shares") to settle certain disputes with a related party, Energy 2000 NGC. As part of the settlement, the related party has agreed to sell the NGS Shares for gross proceeds of at least \$1.25 per share, with the net proceeds after commissions, to be distributed to Verdisys. In addition, as part of the settlement, the Berg McAfee Companies and Eric McAfee have agreed to make an investment of \$200,000 in Verdisys, to be evidenced by convertible promissory notes bearing interest at the rate of 8% per annum with a maturity date of May 31, 2006. The notes would be convertible into common stock at the rate of one (1) share of common stock for each \$2.00 dollars of principal and interest outstanding. Verdisys believes the proceeds from sale of the NGS Shares and the amount received from the convertible promissory note investment will improve the company's cash outlook.

Subsequent Events

Energy 2000

In October, 2004 Verdisys entered into an agreement with Berg McAfee Companies, Energy 2000 NGC, Inc. (Energy 2000), and Eric McAfee to settle several outstanding legal issues. Energy 2000 has agreed to settle a Finders Fee and Lateral Drilling services dispute by delivering 300,000 shares of Natural Gas Systems stock into escrow for Verdisys. The Company plans to have these shares monetized as soon as practical. Furthermore, to settle a contemplated third party legal dispute, Verdisys and the parties have exchanged into escrow 500,000 shares of Natural Gas Systems stock for 500,000 of Verdisys shares and Verdisys has delivered an additional 250,000 shares. Verdisys also has agreed to dismiss the Quikview, Inc. lawsuit, which it had filed against certain individuals.

Lastly, Berg McAfee Companies and Eric McAfee have loaned \$200,000 to Verdisys, to be evidenced by convertible promissory notes bearing interest at the rate of 8% per annum with a maturity date of May 31, 2006. The notes would be convertible into common stock at a conversion rate of one share of common stock for each \$2.00 of principal and interest outstanding.

New Licensing Agreement

Verdisys has signed an exclusive worldwide licensing agreement with Alberta Energy Holdings for the application of their Abrasive Fluid Jet (AFJ) cutting technique to cut through well casing in oil and gas wells. Applications of such cutting techniques are a proven feature in industries as diverse as munitions disposal in the military, offshore platform dismantlement in the salvage industry and cutting specialty glass and steel in the machining industry. Verdisys would be among the first to apply the proven techniques to the energy service business.

Abrasive cutting utilizes high-pressure fluid and a small amount of abrasives, such as garnet sand, up to 20,000 pounds per square inch. It can cut through surfaces as tough as four inches of steel as well as granite. Abrasive cutting represents an off-the-shelf technology requiring application to drilling rather than developing a new invention. The successful application of abrasive cutting should allow Verdisys the ability to add a new service to its product line, such as milling holes and jetting laterals down to 10,000 feet or more instead of the current limitation of 6,000 feet. It may also facilitate cutting slots in well casings - potentially a large value-added application in conventional drilling and completion operations, especially offshore.

During the past few months, Verdisys has been enhancing its' lateral drilling down-hole equipment in an effort to achieve a more consistent milling process with a higher degree of reliability for their customers. After a series of iterative above and below ground tests, these have significantly improved the reliability of the milling process. The Company is now applying similar iterative steps in an effort to improve the reliability of the lateral jetting process, which has a direct impact on potentially improving oil and gas production for the customer. In parallel to these ongoing operations, Verdisys plans to develop and employ abrasive cutting techniques into their future lateral drilling operations. Funding for developing this abrasive cutting into a lateral drilling application is expected to come from ongoing rig revenues, current and future capital commitments. This agreement is subject to approval by the board of directors for Verdisys.

Under the terms of the licensing agreement, Alberta Energy Holdings will earn warrants for Verdisys common stock as specific phases of the AFJ process are successfully applied, a consulting fee during development as well as a royalty fee for each well where AFJ technology is used. Under the terms of the agreement, Alberta is entitled to receive four tranches of warrants. Each tranche will entitled Alberta the right to purchase 250,000 shares of Verdisys common stock, and each award is contingent upon the attainment of certain specific milestones as fully described in the agreement. The warrants will have a three-year term, with a strike price of \$0.50 per share for the first tranche and \$0.62 per share for the remaining tranches. The initial tranche will be fully vested as of the date of the agreement, and the remaining warrants will vest at 31,250 shares per quarter from the date of issuance.

[Table of Contents](#)

Verdisys has agreed to pay Alberta a \$10,000 per month consulting fee for six months beginning on November 30, 2004. In addition, royalties are payable by Verdisys at the rate of \$1,000 per well for services billed at \$40,000 or less, and for services above \$40,000, a royalty of 2% per well is payable quarterly.

The agreement also provides for the mutual sharing of the proceeds from the sale of the technology by Verdisys, subject to a cap of \$10 million.

Item 3. Controls and Procedures

The Company's Principal Executive Officer and Principal Financial Officer have undertaken an evaluation of the Company's disclosure controls and procedures as of September 30, 2004. The Company's Principal Executive Officer and Principal Financial Officer have concluded that the existing disclosure controls and procedures are effective to provide reasonable assurances that the information required to be disclosed by the Company in the reports it files or submits under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms.

Part II. OTHER INFORMATION

Item 1. Legal Proceedings

Full disclosure of prior or other legal activities may be found in the audited financial statements and notes thereto contained in Verdisys' Annual Report filed with the SEC on Form 10-KSB., and in the Quarterly Report on Form 10-Q for the quarter ended March 31 and June 30, 2004, and in the notes to the financial statements in this report.

Item 2. Change in Securities and Use of Proceeds

During the third quarter of 2004, Verdisys borrowed \$350,000 under convertible promissory notes maturing on December 31, 2005 and carrying an interest rate of 8 per cent. The debt is convertible into common stock at \$2.00 per share and attached to the debt were 175,000 warrants to purchase shares of common stock at 1/10th of a penny per share. The notes will be discounted for the relative fair value of the warrants. The investors were accredited investors as defined in Rule 501 of Regulation D promulgated under Section 4(2) of the Securities Act.

The funds raised during the quarter were primarily utilized for working capital purposes.

Item 3. Defaults Upon Senior Securities

None

Item 5. Other Information

Effective as of October 27, 2004, Verdisys entered into a license agreement with Alberta Energy Holdings. In addition, effective November 2, 2004, Verdisys entered in a settlement agreement with Berg McAfee Companies, Energy 2000 NGC and Eric McAfee. The disclosure of each of those items would otherwise be required to be disclosed in a Form 8-K but is included in this report under the heading "Management Discussion and Analysis or Plan of Operation - Subsequent Events."

Item 6. Exhibits and Reports on Form 8-K

Reports on Form 8-K

None

[Table of Contents](#)

Exhibits

Verdisys, Inc. includes herewith the following exhibits.

- 10.1 License Agreement between Alberta Energy Holdings, Inc. and Verdisys, Inc. for Abrasive Fluid Jet Technology, dated October 27, 2004
- 10.2 Agreement between Verdisys, Berg McAfee Companies, Energy 2000 NGC, and Eric McAfee
- 31.1 Certification of Principal Executive Officer pursuant to Section 302
- 31.2 Certification of Principal Accounting Officer pursuant to Section 302
- 32.1 Certification of Principal Executive Officer pursuant to Section 1350
- 32.2 Certification of Principal Accounting Officer pursuant to Section 1350

[Table of Contents](#)

SIGNATURES

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

Verdisys, Inc.

By: /s/ David M. Adams, COO

David M. Adams
Chief Operating Officer
Principal Executive Officer

Date: November 15, 2004

By: /s/ John O'Keefe, CFO

John O'Keefe
Chief Financial Officer
Principal Accounting Officer

Date: November 15, 2004

LICENSE AGREEMENT

Between

ALBERTA ENERGY HOLDINGS, INC

And

VERDISYS, INC.

For

ABRASIVE FLUID JET TECHNOLOGY

October 27, 2004

LICENSE AGREEMENT

ABRASIVE FLUID JET TECHNOLOGY

TABLE OF CONTENTS

ARTICLE I DEFINITIONS	1
ARTICLE II LICENSE GRANT FOR TECHNICAL INFORMATION	3
ARTICLE III CONFIDENTIALITY OF INFORMATION	4
ARTICLE IV LICENSE	4
ARTICLE V REPRESENTATIONS AND WARRANTIES	5
ARTICLE VI ROYALTIES, FEES AND COMMERCIAL ARRANGEMENTS	6
ARTICLE VII PAYMENTS AND REPORTS	7
ARTICLE VIII SUBLICENSING AND SUBCONTRACTING	8
ARTICLE IX FORCE MAJEURE	8
ARTICLE X BEST EFFORTS	9
ARTICLE XI RIGHT OF TERMINATION	9
ARTICLE XII ASSIGNABILITY	10
ARTICLE XIII TERM OF AGREEMENT	12
ARTICLE XIV GOVERNING LAW & ARBITRATION	13
ARTICLE XV MISCELLANEOUS	13

**LICENSE AGREEMENT
ABRASIVE FLUID JET TECHNOLOGY**

THIS AGREEMENT is made and entered into on this 27 day of October, 2004, by and among Alberta Energy Holdings, Inc. a Delaware Corporation having its principal office in Nashville, Tennessee (“AEH”) (herein referred to as “AEH”) or designee; and Verdisys, Inc., a California Corporation having its principal place of business at 14550 Torrey Chase Blvd, Houston, TX 77014 (“Verdisys”) (herein referred to as “VERDISYS”) (collectively referred to as the “Parties” and individually as “Party”).

WHEREAS, AEH owns technical information and Preparatory Designs relating to the Abrasive Fluid Jet Technology (“AFJ” or the “Technology” as more particularly defined herein) which AEH is willing to make available under license to VERDISYS upon the terms herein set forth; and

WHEREAS, AEH desires to have VERDISYS market the design, fabrication, transportation, installation, use and sale of Technology under license; and

WHEREAS, AEH has the exclusive rights to the Technology and which AEH is willing to make available under license to VERDISYS upon the terms herein set forth; and

WHEREAS, VERDISYS desires to develop and market the design, fabrication, transportation, installation, use and sale of Technology under license; and

WHEREAS, AEH desires to grant and VERDISYS desires to obtain a license for the right to use AEH’s Technical Information, including for use in the Licensed Process to design, fabricate, manufacture, store, transport, install, use, sell and market Technology, in connection with the marketing and sale of Technology and to acquire therewith a license under AEH’s Design Rights (herein defined) subject to the terms herein set forth;

NOW, THEREFORE, FOR AND IN CONSIDERATION of the mutual promises and covenants contained herein and for other good and valuable consideration the adequacy and sufficiency of which is hereby acknowledged, the Parties agree as follows:

**ARTICLE I
DEFINITIONS**

1.01 For all purposes of this Agreement, the following definitions shall apply:

(1) The term “Confidential Technical Information” shall mean any and all technical information of the designated Party except:

- (a) technical information which at the time of disclosure is in the public domain;
- (b) technical information which the recipient can show was in its possession at the time of disclosure and it was not acquired, directly or indirectly, from the other Party hereto; or

- (c) technical information which was received by the recipient after the time of disclosure hereunder from a third party who did not acquire it, directly or indirectly, from the disclosure Party under an obligation of confidence.

(2) The term "Licensed Territory" shall mean the entire world, including, but not limited to, the United States of America and all of its territories to which the United States Patent Laws apply. AEH shall also enjoy the right to use the Technology without paying royalties for joint ventures in which AEH participates but under no circumstances will AEH perform services for third parties.

(3) The term "Licensed Process" shall mean the process of design, fabrication, manufacturing, transportation, installation, storing, using, selling and marketing Technology in a manner commercially useful or marketable. The Licensed Process shall include, but not be limited to:

- (a) Descriptions, designs, drawings, and specifications of Technology and associated products; and
- (b) Descriptions, designs, drawings, and specifications for all materials utilized in Technology, and associated products;
- (c) Methods, know how, specifications, and procedures to be employed in the design, manufacturing, fabrication, transportation, installation, storing, using, selling and marketing of Technology and associated products including specifications, tolerances used, techniques, methodologies, procedures and all equipment associated with the design, manufacturing, fabrication, transportation, installation, storing, using, selling and marketing of Technology; and
- (d) All improvements, licensed or acquired technology, developments, or information that otherwise becomes available to AEH during the term of this Agreement related to the items of this paragraph as set out above.

(4) The term "AEH's Design Rights" shall mean Designs and patent applications issued and/or filed in all countries of the world before or during the term of this Agreement to the extent that they or the claims thereof cover one or more features of Licensed Process or the commercial production of Technology (including apparatus and specifications for carrying out the manufacture, fabrication, storage, transportation or use of Technology and associated products therefrom) whether or not such inventions have been in commercial use, and as to which inventions AEH shall have the right at any time to make the grants provided for in this Agreement, without accounting therefor to others, subject to the conditions under which AEH now has or hereafter acquires the right to make the grants provided for in this Agreement. "AEH's Patent Rights" shall also include the patents and applications listed in Schedule A.

The term "AEH's Issued Patents" shall mean any patents issued in any country from patent applications encompassed by AEH's Patent Rights.

(5) The term “Technology” shall mean the Abrasive Fluid Jet process invented by AEH.

(6) The term “Sublicensee” shall have the meaning ascribed to it in Paragraph 10.01.

(7) The term “Field of Use” refers to use of the Party’s Design Rights or technical information in the design, manufacture, storage, transportation, installation use, sale or marketing of Technology.

(8) The term “Intellectual Property” shall mean the Licensed Process and any and all patents and applications, including AEH’s Patent Rights and “know how” and AEH’s Trademarks, including the License Trademark and AEH’s Technical Information and AEH’s Confidential Technical Information or any other information developed by AEH relevant to the License Process.

ARTICLE II
LICENSE GRANT FOR TECHNICAL INFORMATION

2.01 Subject to the provisions of this Agreement, AEH hereby grants to VERDISYS the exclusive, nontransferable (except as hereinafter provided) license, including the right to sublicense others, to use AEH’s Technical Information, including AEH’s Confidential Technical Information throughout the Licensed Territory. AEH and VERDISYS agree to jointly review the full range of VERDISYS’s and AEH’s Technical Information and marketing status of the Technology at least quarterly in order to promote and assist VERDISYS’s sales in the Field of Use throughout the Licensed Territory.

2.02 Subject always to Paragraph 4.02, nothing in this Agreement shall confer upon VERDISYS any right to use AEH’s Confidential Technical Information for any purpose other than disclosure to its Customers and potential Customers upon execution of a confidentiality agreement with VERDISYS or as otherwise set out in Section 3.01 and the design, fabrication, including the right to sublicense others as provided in Paragraph 10.01, storage, transportation, installation, use, manufacture, sale and marketing of Technology (subject to the further limitations of Paragraph 2.01 hereof), and VERDISYS agrees that so long as prohibited by this Agreement it will not, without the prior written permission of AEH, use AEH’s Confidential Technical Information furnished, directly or indirectly, hereunder to VERDISYS for any other purpose. Nothing contained in this Agreement, including this Paragraph 2.02, however, shall operate to deny VERDISYS the right to use for any purpose AEH’s Technical Information or technical information received at any time from a third party.

2.03 Subject to the provisions of this Agreement, AEH agrees to make available it’s Technical Information to VERDISYS, and subject to the prior written consent of AEH which shall not be unreasonably withheld with respect to each prospective license, AEH hereby grants to VERDISYS, together with the right to extend said grant to others who make all of their technical information related to the Technology available to VERDISYS, the nonexclusive, nontransferable, non-assignable license to use AEH’s Technical Information in the practice of the Licensed Process outside of the Field of Use without accounting therefor to AEH, until, but only until, three (3) months following the date that all of AEH’s Patent Rights have expired and

not thereafter, provided, however, that AEH shall always be prohibited from disclosing to as well as using it's Technical Information and VERDISYS's Confidential Technical Information for the benefit of any person or Company that competes with VERDISYS.

2.04 Promptly after being requested to do so by VERDISYS, AEH agrees to make available to VERDISYS, AEH's Technical Information and personnel necessary to train VERDISYS on the use of AEH's Technical Information for a fee. AEH agrees to train key personnel of VERDISYS to impart information, engineering expertise, know how, and the technology necessary or desirable for the design, fabrication, manufacture, storage, transportation, installation, sale and marketing of Technology and associated products. AEH training shall include the training of key personnel of VERDISYS at mutually agreeable times to observe and learn engineering information necessary or desirable for the design, fabrication, storage, transportation, installation, use, manufacture, sale and marketing of Technology in accordance with AEH's Technical Information.

ARTICLE III CONFIDENTIALITY OF INFORMATION

3.01 Subject to the terms of this Agreement, VERDISYS agrees to use its best reasonable efforts to maintain AEH's Confidential Technical Information in confidence and to use its best efforts to prevent the disclosure thereof to others except that VERDISYS, to the extent necessary for VERDISYS's daily operations, including for marketing purposes, such as but not limited to presentations to clients, press releases, presentations to conferences, business forums, and the like, may disclose AEH's Confidential Technical Information to third parties who shall have agreed to the reasonable satisfaction of VERDISYS to maintain same in confidence to the extent required herein of VERDISYS and to use said AEH's Confidential Technical Information only to the extent authorized or from whom VERDISYS cannot obtain appropriate agreements of confidence, but such disclosure is necessary in order to compete.

3.02 VERDISYS agrees to maintain AEH's Confidential Technical Information in confidence and to use its best efforts to prevent the disclosure thereof to others, except that VERDISYS may disclose AEH's Confidential Technical Information to others who are entitled to receive it under Paragraph 2.03 hereof and who shall have agreed to maintain in confidence AEH's Confidential Technical Information to the extent required herein.

3.03 The Parties' obligations to maintain Confidential Technical Information in confidence shall continue until five (5) years following the expiration of AEH's Patent Rights, and thereafter VERDISYS shall be under no further obligation to maintain AEH's Confidential Information in confidence.

ARTICLE IV LICENSE

4.01 Subject to the terms and conditions of this Agreement, AEH hereby grants to VERDISYS an exclusive, nontransferable (except as herein otherwise provided) license, including the right to sublicense under Paragraph 10.1, under AEH's Design Rights to design, fabricate, manufacture, transport, install, use and operate Technology and conduct all supporting activities relating thereto, and to distribute, use, sell and otherwise commercialize Technology in the Field of Use throughout the Licensed Territory.

4.02 Nothing in this Agreement shall prohibit or restrict VERDISYS's right to develop its own inventions unrelated to Technology, to apply for patent and patent such improvements and/or inventions and to hold all rights related to any such patents.

4.03 AEH shall provide VERDISYS with a copy of each issued patent falling within the scope of "AEH'S Issued Patents." For such patents which issue after the effective date of this Agreement, AEH shall provide a copy of such patent to VERDISYS within thirty business days of issuance. For all such patents for which copies are provided by AEH to VERDISYS which contain at least one apparatus claim, AEH shall make or have made a plate containing the word "Patent," followed by the patent number of the issued patent supplied to the VERDISYS. Such plates shall be applied to all products which VERDISYS makes pursuant to the terms of this Agreement after such date of receipt of such issued patent which AEH identifies to VERDISYS are covered by at least one apparatus claim of said patent. VERDISYS shall further request all sublicensees to comply with the marking requirements of this Section.

ARTICLE V REPRESENTATIONS AND WARRANTIES

5.01 AEH hereby makes the following representations and warranties, and AEH acknowledges that each such representation and warranty is material and that VERDISYS has relied thereon in entering into this Agreement:

- (a) AEH is the sole and absolute owner of AEH's Design Rights, AEH's Technical Information and Licensed Trademark, and AEH has the absolute right to grant the licenses herein granted;
- (b) AEH is under no legal restriction and is free to disclose all of AEH's Technical Information and all other technical information of which it is aware related to the Technology as of the date hereof;
- (c) AEH is aware of no prior art that would invalidate its Patent Rights;
- (d) AEH owns AEH's Design Rights outright and free and clear of any and all liens, licenses, transfer agreements, known infringements, known enforceable claims and encumbrances, with the exception of any royalties or profits payable by AEH to the assignors identified in subparagraph 7.01(i) hereof;
- (e) AEH is aware of no asserted claims or demands against AEH's Design Rights or the license herein granted;
- (f) Practicing AEH's Design Rights are not known to infringe any known valid patent, trademark, development, ownership or other proprietary rights of any individual, partnership, corporation or other entity;

- (g) AEH knows of no other product on the market or in development utilizing or substantially similar to AEH's Design Rights and the disclosures therein;
- (h) AEH has obtained all required consents and assignments and has full right, power and authority to license AEH's Design Rights, AEH's Technical Information and Licensed Trademark to VERDISYS in accordance with the terms and conditions contained herein, and VERDISYS may practice the Licensed Process and the design, fabrication, manufacture, transportation, installation, storing, using, selling and marketing in accordance with this Agreement free of any claim or demand on the part of any party.
- (i) AEH shall deliver the AFJ designs and equipment and defined deliverables in the time frame and within the budget as more fully described in Schedule B.

5.02 VERDISYS and AEH agree that this Agreement constitutes a legal, valid and binding obligation for each Party, enforceable against such Party in accordance with its terms (subject always to applicable bankruptcy, insolvency, receivership and other similar laws relating to or affecting the enforcement of creditor's rights generally and to general principles of equity). Further, AEH and VERDISYS warrant and represent to each other:

- (a) that each (i) is duly formed and organized and validly existing under the laws of the jurisdiction of its formation, (ii) is properly qualified to do business and is in good standing under the laws of each jurisdiction in which it does business, (iii) has all necessary corporate or similar power and authority to execute and deliver this Agreement and to consummate the transaction contemplated hereby; and
- (b) that this Agreement, its execution and the fulfillment and compliance with the terms and conditions hereof, do not violate or conflict with any provision of or result in any breach of or default under any (i) organizational documents of each Party, (ii) law or judicial, award, or similar decree, or (iii) agreement, to which parties are bound for their representations and warranties.

**ARTICLE VI
ROYALTIES, FEES AND COMMERCIAL ARRANGEMENTS**

6.01 VERDISYS hereby agrees to pay, or cause to be paid, to AEH a Licensing Fee and Royalty as follows:

- (a) A series of four tranches of 250,000 Verdisys Stock Warrants shall be awarded to AEH tied to achieving key deliverables in the AFT Technology development. [Schedule B] Such awards shall be valid for a three-year term and will have a strike price of \$0.50 per share for the first tranche and \$0.62 cents per share for all remaining tranches. The first tranche of 250,000 shares shall be fully vested upon execution of this agreement. Each remaining tranche will be fully vested at 31,250 shares per quarter from the date of its issue. All shares contain full registration rights and are adjustable for dilution over their term.

- (b) The payment of \$10,000 per month in Consulting Fees for six months. First payment is due November 30, 2004 and monthly thereafter,
- (c) For AFJ services performed on wells billed at \$40,000 or less, a Royalty payment of \$1,000 per well is payable. For AFJ services on wells billed at more than \$40,000, a Royalty payment of two percent of the gross shall be payable. Royalty Payments are based on revenue per well and are due quarterly in arrears at the end of each calendar quarter. Wells serviced become eligible for the payment provision when VERDISYS provides AFJ services to its customers and receives cash payment thereon.
- (d) No additional Licensing Fee or other amounts shall be paid for the Contract Rights, with the exception of the Royalty fees. Upon award of the four tranches of Stock Warrants and interim Consulting Fees, the VERDISYS shall have the right to sublicense for the Contract Rights.

6.02 AEH shall provide full access to the oil and gas acreage that it holds with third parties in Medina County, Texas and to the plant and facilities, rigs and trucks that it owns. VERDISYS may use such wells and acreage for testing and verification procedures with approval of AEH. In the event that the Parties elect to jet lateral wells for the purpose of enhancing production, it is agreed that they shall share the incremental net production income on an equal basis with VERDISYS providing their services at out of pocket cost to AEH.

6.03 In the event of a sale of the Technology LICENSE by the VERDISYS, parties hereby agree to divide the proceeds on a 50/50 basis, however, in no event will AEH receive greater than \$10 million in net proceeds.

6.04 In the event of a sale of a sublicense of the Technology by the VERDISYS, parties hereby agree to divide the proceeds on a 50/50 basis.

6.05 In the event of a sale of the entire Company or business line by the VERDISYS, no division of proceeds is applicable.

6.06 The LICENSE shall automatically renew under this agreement provided that a minimum payment of \$50,000 per year in Royalty payments is paid on a fiscal year basis commencing immediately following commercial deployment of the first mobile drilling unit.

ARTICLE VII PAYMENTS AND REPORTS

7.01 VERDISYS will keep or cause to be kept, in accordance with good accounting practice, books, records and accounts covering its operations hereunder and containing all information necessary for the accurate determination of amounts payable hereunder.

7.02 All payments shall be made by means of a check or wire transfer in US dollars to the bank account designated by AEH.

7.03 In the event any dispute occurs with respect to the royalty obligations of VERDISYS to AEH under this Agreement, both parties shall approve the selection of an independent CPA to audit the books, accounts and records of VERDISYS in accordance with GAAP. Said CPA shall only report the results of such audit and shall not provide any use, sales or marketing backup documentation, customer lists or information, market information, sales projections, customer account data or similar information to any party including AEH. The determination by such independent CPA of the amount of royalties due to AEH, by VERDISYS shall be binding on both Parties. In the event that royalties due to AEH during any calendar year shall have been understated by at least ten percent (10%), VERDISYS shall pay to AEH such understated royalties and pay the cost of such audit. Otherwise, such audit shall be at AEH's expense.

**ARTICLE VIII
SUBLICENSING AND SUBCONTRACTING**

8.01 VERDISYS can subcontract or sublicense for the design, fabrication, manufacture, transportation, storing, use, sales, marketing and/or installation of Technology under this Agreement, or any component or part thereof, irrespective of whether such design, fabrication, manufacture, transportation, storage, usage, sale, marketing and/or installation takes place in Licensed Territory, and for this purpose may disclose AEH's Technical Information to such subcontracting third parties, herein referred to as "Sublicensees", subject to the terms of Article III herein. The use of AEH's Technical Information by Sublicensees must be expressly limited to the design, fabrication, manufacture, transportation, storage, usage, sale, marketing and/or installation of Technology under this Agreement, and no other use of AEH's Technical Information may be made by such Sublicenses.

8.02 The exclusive license granted pursuant to Article V hereof shall also be subject to sublicense by VERDISYS for use in the Field of Use throughout the Licensed Territory, but only to such third parties as to whom AEH shall have been notified and as to whom AEH in its reasonable discretion shall approve, which approval shall not be unreasonably withheld; provided that AEH shall always be prohibited from utilizing such sublicense in any way for the benefit of any person or company that competes with VERDISYS. In the exercise of its discretion, AEH shall consider, but shall not be limited to consideration of, such factors as the reputation for quality, reliability, after-sales service and similar criteria of the proposed Sublicensee.

8.03 AEH shall always be prohibited from granting any license or sublicense in any way for the benefit of any person or company that competes with VERDISYS.

**ARTICLE IX
FORCE MAJEURE**

9.01 If the performance of this Agreement by any Party, or of any obligation under this Agreement, is prevented, restricted or interfered with by reason of war, revolution, civil commotion, acts of public enemies, blockage, embargo, strikes, any law, order, proclamation, regulation, ordinance, demand, or requirement having a legal effect of any government or any judicial authority or representative of any such government or any other act whatsoever, whether

similar or dissimilar to those referred to in this clause which are beyond the reasonable control of the Party affected, then the Party so affected shall, upon giving prior written notice to the other Party, be excused from such performance to the extent of such prevention, restriction, or interference; provided, however, that the Party so affected shall use its best efforts to avoid or remove such causes of nonperformance and shall continue performance hereunder with the utmost dispatch whenever such causes are removed.

**ARTICLE X
BEST EFFORTS**

10.01 VERDISYS hereby covenants and agrees that during the term of this Agreement, VERDISYS will use commercially reasonable efforts to market and sell AFJ services in the Field of Use throughout the Licensed Territory; provided, however, should VERDISYS fail to make any effort to market Technology, AEH shall have the right to notify VERDISYS of such failure and if VERDISYS makes no efforts to remedy such failure within six (6) months, AEH shall have the right to terminate this agreement.

10.02 VERDISYS shall have no obligation to invest time or money in the development of Technology beyond the funding of the 6,000 foot depth mobile drilling unit.

**ARTICLE XI
RIGHT OF TERMINATION**

11.01 Except as limited herein immediately below, and except as provided elsewhere, either Party shall have the right to terminate this Agreement following the expiration of ninety (90) Days from written notification of default by one Party to the other and without cure of the default. For the purposes of this Agreement, it shall be deemed an act of default should any Party seek protection from its creditors through a declaration of bankruptcy or insolvency or by reorganization under any of the Bankruptcy laws of the United States.

AEH shall have no right to terminate this Agreement except for VERDISYS's 1) declaration of bankruptcy as prescribed by law, 2) failure to make payment due and owing under this Agreement, or 3) failure to market Technology as set forth in Paragraph 12.01.

11.02 Any termination of the Agreement shall not:

- (a) release VERDISYS or AEH from any claim of the other accrued hereunder prior to the effective date of such termination;
- (b) release VERDISYS or AEH from their obligations under Paragraphs 3.01, 3.02 and 3.03, respectively, unless otherwise released by the further terms hereof;
- (c) affect in any way any rights and immunities made available prior to the effective date of such termination by VERDISYS to AEH or through AEH to others under the provisions of Paragraph 2.03 hereof but subject to the terms and limitations hereof.

- (d) affect or impair VERDISYS's rights and immunities with respect to the commercial practice of Licensed Process to the extent that VERDISYS, prior to the effective date of such termination, may have acquired from AEH any fully paid rights; provided, however, that VERDISYS shall have ninety (90) Days following the date of termination of this Agreement to acquire fully paid licenses by payment to AEH of the amount of royalties due therefor under the terms hereof, or
- (e) release AEH from any obligations to VERDISYS under Article XIV hereof regardless of whether any such liability or action has accrued or been filed or asserted as of the date of termination of this Agreement.

11.03 Upon termination of this Agreement, AEH shall remain the sole owner of the Licensed Trademarks and goodwill associated therewith and VERDISYS shall assert no rights thereto and shall discontinue the use thereof; provided, however, that for a period of one (1) year after termination of this Agreement, or such longer period as shall be reasonably necessary, VERDISYS may continue to use Technology pursuant to the terms of this Agreement on any contract executed by VERDISYS prior to termination of this Agreement. VERDISYS expressly recognizes that it is obligated to continue to comply with Paragraph 5.03 of this Agreement for any period of time that it uses the Technology trademark. VERDISYS and AEH agree that this clause and the obligations thereunder shall survive the termination of this Agreement.

ARTICLE XII ASSIGNABILITY

12.01 This Agreement shall not be assignable to any successor of the entire right, title and interest to that portion of the business of VERDISYS to which this Agreement relates without express written approval of the AEH, such approval not to be unreasonably withheld. When assigned in accordance with this Paragraph, this Agreement and all rights, obligations and duties hereunder will inure to the benefit of and will be binding on the assignees or successors in interest of VERDISYS.

12.02 This Agreement shall not be assigned or transferred by AEH, without the express prior written consent of VERDISYS.

12.03 If any of the shares, voting rights, membership interests or other indicia of ownership ("Interest") of AEH are, or may be, sold, assigned, conveyed, transformed, transferred, diluted, including by options, or exchanged, including by merger, pledged, subjected to any power of attorney or any control by a trust or in any other way alienated in whole or in part to any extent from the current owners as of the date of execution of this Agreement for any reason, or if any of the assets related to the Technology are sold, assigned, conveyed, pledged or transferred in any way except to VERDISYS (collectively "Transfer"), then AEH shall: 1) notify VERDISYS at least ninety (90) Days prior thereto, and 2) shall furnish VERDISYS with all of the terms and conditions associated with such proposed Transfer, and 3) shall offer all of the Contract Rights to VERDISYS, including interests in this License Agreement, the Licensed Process, AEH's Confidential Technical Information, AEH's Technical Information, AEH's Patent Rights, Licensed Trademark, and associated goodwill on the terms of Paragraph 14.05. Nothing herein shall be construed to prevent the owners of the AEH to redistribute their ownership interests in AEH to each other but not to any third parties.

12.04 If VERDISYS fails to market Technology after notice as provided in Paragraph 12.01, then AEH shall have the right to terminate this Agreement.

12.05 Any purported Transfer of any Interest by AEH shall give VERDISYS, and VERDISYS shall have, the option right to purchase the Contract Rights owned by AEH in accordance with the following provisions of this Paragraph 14.05.

- (a) For a period of sixty (60) Days following the VERDISYS's receipt of notice from AEH of a purported Transfer, VERDISYS shall have the first right of refusal to purchase the Contract Rights. If VERDISYS exercises its option to purchase the Contract Rights, the Contract Rights shall be assigned, sold, transferred and conveyed free and clear of all liens, claims or other encumbrances, The purchase shall be closed within thirty (30) Days of written notice from VERDISYS to purchase the Contract Rights except that if a legal impediment exists which prevents the AEH from effectively assigning title to the Contract Rights, then such date of closing shall be extended until any such legal impediment is removed, so long as the person responsible for having such impediment removed continues diligently and in good faith to remove same. Payment of the Value will be made in cash at closing.
- (b) In the event that VERDISYS does not elect to purchase the Contract Rights subject to this Article XIV within the time periods specified therein, the purported Transfer shall not be null, void, and ineffective and shall operate to transfer the Interest to the purported transferee so long as AEH shall not have assigned the Contract Rights to VERDISYS prior thereto in accordance with the terms of this Article XIV.

12.06 A person acquiring any Interest of AEH shall acquire such Interest only upon such person's compliance with the other applicable provisions of this Agreement, including, without limitation, Article XIV. The AEH shall not at anytime hypothecate or otherwise create or suffer to exist any lien, claim or other encumbrance on any Contract Right.

12.07 In the event that a AEH or any of its Interest holders violates, or attempts to threaten to violate, the requirements of this Article XIV, VERDISYS shall, to the extent permitted by applicable law, be entitled to (i) obtain injunctive relief, (ii) obtain a decree compelling specific performance, and/or (iii) obtain any other remedy legally allowed to them.

12.08 If Interest that is covered by this Article XIV is purportedly subject to a Transfer in a transaction that is not in compliance with the requirements of this Article XIV, such purported Transfer shall be void and have no force or effect.

12.09 The Parties hereby declare that it is impossible to measure in money the damages which will accrue to AEH by reason of a failure to perform any of the obligations under this Agreement. Therefore, if any Party shall institute any action or proceeding to specifically enforce

the provisions of this Agreement, any person (including the Company) against whom such action or proceeding is brought hereby waives the claim or defense that such Party or such personal representative has an adequate remedy at law, and such person shall not urge in any such action or proceeding the claim or defense that such remedy at law exists.

12.10 Unless otherwise provided in this Agreement, none of the Parties to this Agreement shall assign, transfer or sublet the Agreement, any portion thereof or any of the obligations, benefits or interest contained therein or created thereby in any manner whatsoever without the prior written consent of all of the other Parties.

12.11 Except as specifically provided for elsewhere herein, this Agreement shall not be construed to confer any benefit on any third party or owners of AEH not a party to this Agreement nor shall it provide any rights to such third party or owner to enforce its provisions.

ARTICLE XIII TERM OF AGREEMENT

13.01 Unless sooner terminated as hereinabove provided, this Agreement shall continue in effect for a term of ten (10) years from the date of filing of the patent application in definition (13), automatically extendable for additional terms of two (2) years each unless at least thirty (30) Days prior to the expiration of any term VERDISYS notifies AEH by registered mail or overnight courier that they elect not to extend this Agreement for such additional period, in which cases this Agreement shall terminate; provided, however, that VERDISYS may continue to use Technology pursuant to the terms of this Agreement on any contract executed by VERDISYS prior to termination of this Agreement, but after the finding of invalidity or unenforceability of all of the AEH's Patent Rights, VERDISYS shall have no further obligation or duty to make royalty payments.

**ARTICLE XIV
GOVERNING LAW AND ARBITRATION**

14.01 THE PARTIES HERETO AGREE THAT THE VALIDITY AND INTERPRETATION OF THIS AGREEMENT AND THE LEGAL RELATIONS OF THE PARTIES HERETO SHALL BE GOVERNED BY THE LAWS OF THE STATE OF TEXAS. THE PARTIES FURTHER ACKNOWLEDGE AND AGREE THAT THIS AGREEMENT WAS NEGOTIATED, CONSUMATED AND ENTERED INTO IN THE CITY OF HOUSTON, STATE OF TEXAS, AND THE PARTIES HEREBY CONSENT TO VENUE IN THE FEDERAL AND STATE COURTS OF COMPETENT JURISDICTION LOCATED IN HOUSTON, TEXAS.

14.02 All claims, disputes or controversies arising out of, in connection with or in relation to this Agreement shall be decided by arbitration in accordance with the Commercial Rules of the American Arbitration Association then in force. For claims, disputes or controversies which either Party may have in excess of \$1,000,000, exclusive of claims for interest, attorneys' fees and costs, three (3) neutral arbitrators shall be used. Otherwise a single arbitrator shall be used. For purposes of determining the number of arbitrators, the Parties claims and counterclaims shall not be additive. The arbitration shall be conducted in Houston, Texas, The decision of the arbitrator(s) shall be final, binding and enforceable in any court of competent jurisdiction and the Parties agree that there shall be no appeal from the arbitrator(s)' decision except s provided by applicable law. All statues of limitation that would otherwise be applicable shall apply to any arbitration proceeding. The right to arbitrate shall survive the termination of this Agreement. The Parties acknowledge and agree that this Agreement includes activities in Interstate Commerce and that the Federal Arbitration Act, 9 USC §1 *et seq* shall control and apply to all arbitrations conducted hereunder, notwithstanding any state law provisions to the contrary.

14.03 The Parties irrevocably agree to be joined as parties in any arbitration proceeding which involves claims, disputes or controversies which either Party may have with other parties not a Party to this Agreement who are also governed by an arbitration agreement.

14.04 The Parties hereby irrevocably waive any objection to the joinder of other parties who are not Parties to this Agreement to any arbitration proceeding commenced pursuant to Section 17.02 above where such other parties are also governed by an arbitration agreement.

**ARTICLE XV
MISCELLANEOUS**

15.01 This Agreement contains the entire and only agreement between the Parties hereto relating to the grant of a license for the Licensed Process, and this Agreement supersedes all pre-existing or prior agreements of the Parties hereto respecting any portion or in any way related to the subject matter of this Agreement. Any representation, promise or condition in connection with the subject matter of this Agreement which is not specifically incorporated in this Agreement, whether written or oral, shall not be binding upon the Parties hereto.

15.02 If, in any legal proceeding, it is determined that any provision of this Agreement is unenforceable under applicable law, the unenforceable provision shall automatically be amended to conform to that which is enforceable under the law. In any event, the validity or enforceability of any provision shall not affect any other provision of this Agreement, and the Agreement shall be construed and enforced as if such provision had not been included.

15.03 No benefit or right accruing to either Party under this Agreement shall be waived unless the waiver is reduced to writing and signed by all Parties to this Agreement. The failure of any Party to exercise any of its rights under this Agreement shall in no way constitute a waiver of those rights, nor shall such failure excuse the other Parties from any of its or their obligations under this Agreement.

15.04 This Agreement shall be binding upon and inure to the benefit of the Parties and Owners therein, their respective successors and permitted assigns.

15.05 The effective date of this agreement shall be the date of execution.

15.06 This agreement is subject to the approval of the Verdisys board of directors,

15.07 Any notice given or required to be given under this Agreement shall be in writing and shall be addressed to the Parties executing this agreement as below:

IN WITNESS WHEREOF, the Parties hereto have respectively caused this Agreement to be executed by their duly authorized representatives as of the date first written above.

AEH (ALBERTA ENERGY HOLDINGS)

By: _____

Witness: _____

Name: Mark McAfee
Title: President & CEO
Date: _____

LICENSEE (VERDISYS)

By: _____

Witness: _____

Name: David Adams
Title: President & Co-CEO
Date: _____

SCHEDULE A

LIST OF PATENTS AND APPLICATIONS INCLUDED IN

AEH's PATENT RIGHTS

A-1

SCHEDULE B

PHASE I - RESOLVE MAJOR PROBLEMS WITH CURRENT MECHANICAL MILLING TECHNOLOGY

Deliverables

- A reliable and predictable milling and jetting process with the down hole equipment
- Surface and down hole verification methods to measure the results of the lateral drilling services
- Surface and field testing of equipment and processes
- AEH earn tranche 1 stock warrants

PHASE II - DEVELOP AFJ MECHANICAL MILLING CAPABILITY WITH AUTO DRIVE & TRAILER UNIT (6,000 FT DEPTH)

Deliverables

- Design and repackaging of proven AFT surface equipment for the use in oil and gas wells
- Design for an automated surface drive system
- Design for high pressure jetting of oil and gas reservoir
- Testing of the automated surface drive system
- Surface and field testing of the high pressure jetting process
- AEH earn tranche 2 stock warrants

PHASE III - DEPLOY PHASE II INTO FIELD TESTING TO VALIDATE TECHNOLOGY DESIGN & OPERATING RANGES

Deliverables

- Validate the AFT design, equipment, and process with controlled surface testing
- Validate the AFT design, equipment, and process in the field on client projects
- AEH earn tranche 3 stock warrants

PHASE IV - DEVELOP AFJ JETTING CAPABILITY & DETAILED ENGINEERING DESIGN TO BUILD AN INTEGRATED MOBILE DRILLING UNIT (10,000 FT DEPTH)

Deliverables

- Detailed design and engineering drawings associated with a new rig system

-
- Definitive budget estimate for the new rig system
 - Detailed bid package for construction of the new rig system
 - AEH earn tranche 4 stock warrants

**PHASE V - BID, EVALUATE & BUILD AN INTEGRATED MOBILE DRILLING
UNIT FOR FIELD DEPLOYMENT**

Deliverables

- Evaluate competitive bids for rig construction
- Let the contract to successful bidder
- Build and take delivery of the rig
- AEH to consult in this phase

**Agreement between Verdisys, Berg McAfee Companies, Energy 2000 NGC,
and Eric McAfee**

The following sets forth the general terms for resolution of certain issues between Verdisys, Inc.; Energy 2000 NGC, Inc.; Berg McAfee Companies, LLC; and Eric McAfee, as an individual:

EDGE CAPITAL:

- The parties acknowledge that the Memorandum of Understanding for the settlement amongst Edge Capital, Verdisys and certain other parties has been executed.
- Eric McAfee or his designee(s), will exchange with Verdisys an aggregate of 500,000 Natural Gas Systems, Inc. shares for 500,000 Verdisys common shares with registration rights. The Verdisys shares shall be included for registration on the current SB-2 filing. These NGS shares shall be deposited by McAfee into an escrow account with Adams & Reese, or designee, pursuant to an escrow agreement and then sold to investors at \$1.25 per share or better to generate a net target of \$625,000 of cash. Verdisys shall not be responsible for arranging the sale of the NGS shares; McAfee will use his best efforts to arrange the sale of the NGS stock in a timely fashion. Some \$625,000 of the cash proceeds from the sale shall be distributed from the escrow to Edge Capital and related parties as provided by the Edge Capital settlement agreement; and the balance, if any, reverts to Verdisys, Inc.
- Verdisys will deliver as newly issued common stock the 250,000 Verdisys common shares into escrow for Edge Capital and related parties per the Edge settlement agreement, including registration rights.

ENERGY 2000:

- Eric McAfee will make an advance to Energy 2000 in the form of 300,000 NGS shares. Energy 2000 will transfer these 300,000 Natural Gas Systems shares to Verdisys as full payment for all amounts currently owed by Energy 2000 to Verdisys for drilling services, third party costs and any other amounts. These NGS shares shall be deposited by Energy 2000 into escrow pursuant to the escrow agreement described above. Verdisys shall not be responsible for arranging the sale of the NGS shares; McAfee will use his best efforts to arrange for the sale of the NGS stock in a timely fashion at a target price of \$1.25 per share or better. The net cash proceeds, after brokerage fees, shall be distributed from the escrow to Verdisys.
- Any further services provided to Energy 2000 by Verdisys, or by a third party hired by Verdisys, shall require the prior written approval of an authorized officer or director of Energy 2000.
- The Master Services Agreement, including the First Amendment, between Energy 2000 and Verdisys shall be amended to remove any reference to revenue sharing.

QUIKVIEW:

- Verdisys will dismiss the Quikview lawsuit against all defendants, with prejudice and the parties to this agreement will sign a general waiver and release to include Verdisys, Quikview, and the named parties to the lawsuit.
- Verdisys acknowledges that on or before November 15, 2004 Berg McAfee Companies will donate to charity the 230,000 Verdisys shares received by Berg McAfee Companies from the Quikview transaction.

INVESTMENT:

- Berg McAfee Companies will make an investment of \$200,000 into Verdisys on the same terms and in a pro rata security position with the recent Linden and Brown notes, with maturity on May 31, 2006. Such investment will be made on or before this Friday October 29, 2004, or as soon thereafter as possible.
- Chadbourn Securities, a NASD broker dealer, shall be retained by Verdisys to arrange the funding of \$1.3 million for working capital and the development of the abrasive cutting technology. Chadbourn shall receive a fee of 8% and an unallocated expense reimbursement of 2% on amounts funded. The Chadbourn fee shall exclude any funds invested by Berg McAfee Companies. Verdisys will provide reasonable investor presentation documentation and other support in order to raise this funding in November 2004.

This Agreement states the intentions of the parties, is fully binding, and is subject to the laws of the State of Texas. The effective date is October 27, 2004.

Berg McAfee Companies:

Verdisys, Inc.:

Eric McAfee, Managing Member
Berg McAfee Companies, LLC

John O'Keefe, Chief Financial Officer
Verdisys, Inc.

Energy 2000:

Eric McAfee:

Richard Thompson, CEO
Energy 2000 NGC, Inc.

Eric McAfee, as an individual

CERTIFICATION

I, David M. Adams, certify that:

- 1) I have reviewed this quarterly report on Form 10-QSB of Verdisys, Inc.;
- 2) Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
- 3) Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the small business issuer as of, and for, the periods presented in this report;
- 4) The small business issuer's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the small business issuer and have:
 - a. designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the small business issuer, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b. evaluated the effectiveness of the small business issuer's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - c. disclosed in this report any change in the small business issuer's internal control over financial reporting that occurred during the small business issuer's most recent fiscal quarter (the small business issuer's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the small business issuer's internal control over financial reporting; and
- 5) The small business issuer's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the small business issuer's auditors and the audit committee of small business issuer's board of directors (or persons performing the equivalent functions):
 - a. all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the small business issuer's ability to record, process, summarize and report financial information; and
 - b. any fraud, whether or not material, that involves management or other employees who have a significant role in the small business issuer's internal controls over financial reporting.

Date: November 15, 2004

/s/ David M. Adams

David M. Adams
Co-Chief Executive Officer
Chief Operating Officer
Principal Executive Officer

CERTIFICATION

I, John O'Keefe, certify that:

- 1) I have reviewed this quarterly report on Form 10-QSB of Verdisys, Inc.;
- 2) Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
- 3) Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the small business issuer as of, and for, the periods presented in this report;
- 4) The small business issuer's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the small business issuer and have:
 - a. designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the small business issuer, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b. evaluated the effectiveness of the small business issuer's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - c. disclosed in this report any change in the small business issuer's internal control over financial reporting that occurred during the small business issuer's most recent fiscal quarter (the small business issuer's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the small business issuer's internal control over financial reporting; and
- 5) The small business issuer's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the small business issuer's auditors and the audit committee of small business issuer's board of directors (or persons performing the equivalent functions):
 - a. all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the small business issuer's ability to record, process, summarize and report financial information; and
 - b. any fraud, whether or not material, that involves management or other employees who have a significant role in the small business issuer's internal controls over financial reporting.

Date: November 15, 2004

/s/ John O'Keefe

John O'Keefe
Co-Chief Executive Officer
Chief Financial Officer
Principal Accounting Officer

**CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Quarterly Report on Form 10-QSB of Verdisys, Inc. (the "Company") for the period ended September 30, 2004 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, David M. Adams, Co-Chief Executive Officer, Chief Operating Officer and Principal Executive Officer of the Company, certify pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

- (1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: November 15, 2004

By: /s/ David M. Adams

David M. Adams
Co - Chief Executive Officer
Chief Operating Officer
Principal Executive Officer

**CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Quarterly Report on Form 10-QSB of Verdisys, Inc. (the "Company") for the period ended September 30, 2004 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, John O'Keefe, Co-Chief Executive Officer, Chief Financial Officer and Principal Accounting Officer of the Company, certify pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

- (1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: November 15, 2004

By: /s/ John O'Keefe

John O'Keefe
Co-Chief Executive Officer Chief
Financial Officer
Principal Accounting Officer