

Pharma-Bio Serv, Inc.
Form 10QSB
June 14, 2007

**UNITED STATES
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 April 30, 2007

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

For the transition period from _____ to _____

Commission File No. 000-50956

PHARMA-BIO SERV, INC.
(Name of small business issuer as specified in its charter)

Delaware
(State of Incorporation)

20-0653570
(I.R.S. Employer
Identification No.)

373 Méndez Vigo, Suite 110, Dorado, Puerto Rico 00646
(Address of principal executive offices)

787-278-2709
(Issuer's telephone number)

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

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). yes no

The number of shares outstanding of the registrant's Common Stock as of June 12, 2007 was 19,615,539.

PHARMA-BIO SERV, INC.

FORM 10-QSB

FOR THE QUARTER ENDED APRIL 30, 2007

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PHARMA-BIO SERV, INC.
Consolidated Balance Sheet (Unaudited)
As of April 30, 2007

Assets:	
Current assets	
Cash and cash equivalents	\$ 3,309,531
Accounts receivable	3,971,261
Other	216,563
Total current assets	7,497,355
Property and equipment	
	314,484
Other assets, mainly intangible assets	
	168,391
Total Assets	\$ 7,980,230
Liabilities and Stockholders' Equity:	
Current liabilities	
Current portion-obligations under capital leases	\$ 40,430
Accounts payable and accrued expenses	1,330,779
Due to affiliate - current	2,613,225
Income taxes	364,128
Total current liabilities	4,348,562
Long-term liabilities	
Due to affiliate	2,450,465
Other long-term liabilities	121,043
Total long-term liabilities	2,571,508
Total Liabilities	6,920,070
Stockholders' Equity:	
Preferred Stock, \$0.0001 par value; authorized 10,000,000 shares; none outstanding	-
Common Stock, \$0.0001 par value; authorized 50,000,000 shares; issued and outstanding 19,615,539 shares	1,961
Additional paid-in capital	65,374
Retained earnings	992,825
Total Stockholders' Equity	1,060,160
Total Liabilities and Stockholders' Equity	\$ 7,980,230

See notes to financial statements.

PHARMA-BIO SERV, INC.
Consolidated Statements of Income (Unaudited)
For the Three-Month Periods and the Six-Month Periods Ended April 30, 2007 and 2006

	Three months ended April 30,		Six months ended April 30,	
	2007	2006	2007	2006
REVENUES	\$ 4,180,562	\$ 3,804,703	\$ 7,798,892	\$ 7,208,885
COST OF SERVICES	2,362,277	2,233,166	4,529,405	4,266,505
GROSS PROFIT	1,818,285	1,571,537	3,269,487	2,942,380
SELLING, GENERAL AND ADMINISTRATIVE EXPENSES	829,672	567,243	1,566,257	1,019,229
INTEREST EXPENSE	84,556	130,734	213,802	134,146
INCOME BEFORE INCOME TAX	904,057	873,560	1,489,428	1,789,005
INCOME TAX	385,745	398,305	641,700	420,178
NET INCOME	\$ 518,312	\$ 475,255	\$ 847,728	\$ 1,368,827
BASIC EARNINGS PER COMMON SHARE	\$ 0.03	\$ 0.14	\$ 0.04	\$ 0.53
DILUTED EARNINGS PER COMMON SHARE	\$ 0.02	\$ 0.02	\$ 0.04	\$ 0.10
WEIGHTED AVERAGE NUMBER OF COMMON SHARES OUTSTANDING - BASIC	19,615,539	3,381,342	19,162,866	2,573,492
WEIGHTED AVERAGE NUMBER OF COMMON SHARES OUTSTANDING - DILUTED	22,120,730	22,066,604	21,897,862	13,610,896

See notes to financial statements.

PHARMA-BIO SERV, INC.
Consolidated Statements of Cash Flows (Unaudited)
For the Three-Month Periods and the Six-Month Periods Ended April 30, 2007 and 2006

	Three months ended April 30,		Six months ended April 30,	
	2007	2006	2007	2006
CASH FLOWS FROM OPERATING ACTIVITIES:				
Net income for the period	\$ 518,312	\$ 475,255	\$ 847,728	\$ 1,368,827
Loss on disposition of property and equipment	5,798	-	25,661	3,664
Stock-based compensation	26,352	-	65,374	-
Depreciation and amortization	53,160	58,796	107,657	88,940
Imputed interest expense	82,118	127,216	208,729	127,216
Decrease (increase) in accounts receivable	23,370	(1,493,829)	1,784,616	(12,037)
Decrease (increase) in other assets	200,876	(135,728)	249,536	(286,033)
Increase (decrease) in liabilities	243,834	146,218	532,323	(3,704)
NET CASH PROVIDED BY (USED IN) OPERATING ACTIVITIES	1,153,820	(822,072)	3,821,624	1,286,873
CASH FLOWS FROM INVESTING ACTIVITIES:				
Purchase of property and equipment	(7,859)	(3,656)	(18,080)	(90,684)
Cash acquired as part of the acquisition of Plaza	-	-	-	28,943
NET CASH USED IN INVESTING ACTIVITIES	(7,859)	(3,656)	(18,080)	(61,741)
CASH FLOW FROM FINANCING ACTIVITIES:				
Net proceeds from the sale of preferred stock	-	-	-	10,000,000
Payment for purchase of stock in Plaza	-	-	-	(9,900,000)
Payment for non-compete covenant	-	-	-	(100,000)
Payments on capital lease obligations	(9,622)	(8,542)	(19,048)	(17,191)
Payments to affiliate	(250,000)	-	(2,750,000)	-
Distributions	-	-	-	(749,554)
NET CASH USED IN FINANCING ACTIVITIES	(259,622)	(8,542)	(2,769,048)	(766,745)
NET INCREASE (DECREASE) IN CASH	886,339	(834,270)	1,034,496	458,387
CASH - BEGINNING OF PERIOD	2,423,192	3,084,214	2,275,035	1,791,557

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CASH - END OF PERIOD	\$	3,309,531	\$	2,249,944	\$	3,309,531	\$	2,249,944
PAYMENTS OF:								
Income tax	\$	150,000	\$	364,063	\$	150,000	\$	364,063
Interest	\$	5,073	\$	3,518	\$	508,781	\$	6,930
NONCASH INVESTING AND FINANCING ACTIVITIES:								
Conversion of preferred stock to common stock	\$	-	\$	1,483	\$	-	\$	1,483
Conversion of cashless exercise warrants to shares of common stock	\$	-	\$	-	\$	130	\$	-
Income tax withheld by clients but used as a credit in the income tax return of a stockholder (noncash distribution)	\$	-	\$	-	\$	-	\$	84,561
Income tax withheld by clients to be used as a credit in the Company's income tax return	\$	45,212	\$	-	\$	53,573	\$	-
Debt incurred in the acquisition of certain assets from a validation company	\$	-	\$	-	\$	-	\$	200,000
Debt payable to officer originated in the acquisition of Plaza Plaza, net of \$1,025,000 imputed interest	\$	-	\$	-	\$	-	\$	7,225,000

See notes to financial statements.

PHARMA-BIO SERV, INC.
Consolidated Statement of Changes in Stockholders' Equity (Unaudited)
For the Six-Month Period Ended April 30, 2007

	Common Stock		Preferred Stock		Additional	Retained	Total
	Shares	Amount	Shares	Amount	Paid-in Capital	Earnings	
BALANCE AT OCTOBER 31, 2006	18,315,001	\$ 1,831	-	\$ -	-	\$ 145,227	\$ 147,058
CASHLESS CONVERSION OF WARRANTS TO SHARES OF COMMON STOCK	1,300,538	130	-	-	-	(130)	-
STOCK-BASED COMPENSATION					65,374		65,374
NET INCOME	-	-	-	-	-	847,728	847,728
BALANCE AT APRIL 30, 2007	19,615,539	\$ 1,961	-	\$ -	65,374	\$ 992,825	\$ 1,060,160

See notes to financial statements.

PHARMA-BIO SERV, INC.
Notes to Consolidated Financial Statements (Unaudited)
For the Three-Month Periods and the Six-Months Periods Ended April 30, 2007 and 2006

NOTE A - ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

BASIS OF PRESENTATION

Pharma-Bio Serv, Inc. ("Pharma-Bio") is a Delaware corporation organized on January 14, 2004, under the name Lawrence Consulting Group, Inc. ("Lawrence"). Pharma-Bio is the parent company of Plaza Consulting Group, Inc. ("Plaza"), a Puerto Rico corporation, which operates in Puerto Rico and the United States under the name of Pharma Serv and is engaged in providing technical compliance consulting services primarily to the pharmaceutical, chemical, medical device and biotechnology industries. Pharma-Bio and Plaza are collectively referred to as the "Company".

On January 25, 2006, Pharma-Bio acquired Plaza in a transaction that is accounted for as a reverse acquisition. Although Pharma-Bio, then known as Lawrence, is the corporation that made the acquisition, for accounting purposes, Plaza is treated as the acquiring company. As a result, the financial statements reflect the results of operations and cash flows of Plaza prior to January 25, 2006 and the consolidated financial position and results of operations of Pharma-Bio and Plaza from and after January 25, 2006.

All intercompany transactions and balances have been eliminated in consolidation.

The unaudited interim financial statements for the three-month periods and the six-month periods ended on April 30, 2007 and 2006 presented herein have been prepared in accordance with accounting principles generally accepted in the United States for interim financial statements and with the instructions to Form 10-QSB and Regulation S-B pertaining to interim financial statements and reflect all adjustments, consisting of normal recurring adjustments and accruals which, in the opinion of management, are considered necessary for a fair presentation of the Company's financial position, results of operations and cash flows. Results of operations for interim periods are not necessarily indicative of the results that may be expected for the full year.

REVERSE ACQUISITION

On January 25, 2006, pursuant to a plan and agreement of merger (the "Plaza Agreement") dated as of October 31, 2005, among Pharma-Bio, Plaza Acquisition Corp., a wholly-owned subsidiary of Pharma-Bio ("Acquisition Company"), Plaza and Elizabeth Plaza, the sole stockholder of Plaza, Pharma-Bio acquired Plaza. The acquisition was effected by the merger of Acquisition Company into Plaza. Pursuant to the Plaza Agreement, Ms. Plaza, as the sole stockholder of Plaza, received at the closing \$10,000,000 plus 1,150,000 shares of Pharma-Bio's common stock. In addition, the Plaza Agreement provides for the Company to make three annual payments to Ms. Plaza, each in the amount of \$2,750,000, payable on January 25, 2007, 2008 and 2009. See Note G with respect to payments made and obligations due to affiliate.

At the closing, all of the present officers and directors of Pharma-Bio resigned from their respective positions, except that Mr. Dov Perlysky, who was president and a director of Pharma-Bio, resigned as an officer, but continued as a director. At the closing, Pharma-Bio elected four directors, including Ms. Plaza. The other three are independent directors.

Pharma-Bio raised the funds necessary to make the \$10,000,000 payment due to Ms. Plaza through the private placement of units consisting of shares of a series A preferred stock and warrants to purchase 7,999,400 common stock. The series A preferred stock was automatically converted into 15,998,800 shares of common stock upon an increase in Pharma-Bio's authorized common stock. See Note C.

The acquisition of Plaza and the private placement resulted in a change of control of Pharma-Bio. As a result of the reverse acquisition accounting treatment, Plaza is deemed to be the acquiring company for accounting purposes. The transaction was accounted for as a reverse acquisition because former owners of Plaza, together with the purchasers in the private placement who purchased the series A preferred stock and warrants in connection with the acquisition of Plaza, gained control of Pharma-Bio. Effective on the acquisition date, Pharma-Bio's balance sheet includes the assets and liabilities of Plaza and its equity accounts have been recapitalized to reflect the equity of Pharma-Bio.

SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Use of Estimates

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

Fair Value of Financial Instruments

The carrying value of the Company's financial instruments (excluding obligations under capital leases and amounts due to affiliate): cash, accounts receivable, accounts payable and accrued liabilities, are considered reasonable estimates of fair value due to the short-term nature. Management believes, based on current rates, that the fair value of its obligations under capital leases and amounts due to affiliate approximate the carrying amount.

Revenue Recognition

Revenue is primarily derived from: (1) time and materials contracts (representing approximately 90% of total revenues), which is recognized by applying the proportional performance model, whereby revenue is recognized as performance occurs, and (2) short-term fixed-fee contracts or "not to exceed" contracts (approximately 10% of total revenues), which revenue is recognized similarly, except that certain milestones also have to be reached before revenue is recognized. In the case of fixed-fee contracts, which mostly are short-term contracts, revenue is recognized based on the percentage that the services rendered bears to the estimated services to be performed over the contract. If the Company determines that a fixed-fee or "not to exceed" contract will result in a loss, the Company recognizes the estimated loss in the period in which such determination is made.

Cash and Cash Equivalents

For purposes of the statements of cash flows, cash and cash equivalents include liquid investments with original maturities of three months or less.

Accounts Receivable

Accounts receivable are recorded at their estimated realizable value. Accounts are deemed past due when payment has not been received within the stated time period. The Company's policy is to review individual past due amounts periodically and write off amounts for which all collection efforts are deemed to have been exhausted. Due to the nature of the Company's customers, bad debts are accounted for using the direct write-off method whereby an expense is recognized only when a specific account is determined to be uncollectible. The effect of using this method approximates that of the allowance method.

Income Taxes

The Company follows the provisions of Statement of Financial Accounting Standards Board No. 109, "Accounting for Income Taxes," which requires an asset and liability approach method of accounting for income taxes. This method measures deferred income taxes by applying enacted statutory rates in effect at the balance sheet date to the differences between the tax basis of assets and liabilities and their reported amounts on the financial statements. The resulting deferred tax assets or liabilities are adjusted to reflect changes in tax laws as they occur. A valuation allowance is provided when it is more likely than not that a deferred tax asset will not be realized.

Plaza, from its inception until January 24, 2006, was covered under the provisions of Subchapter N of Subtitle A of the Puerto Rico Internal Revenue Code (the "Puerto Rico Code"), which is similar to Subchapter S of the Internal Revenue Code in that its taxable income is taxed to the stockholders and therefore there is no income tax liability for that period. As a result of the completion of the reverse acquisition, Plaza and Pharma-Bio are no longer eligible for treatment as a Subchapter N corporation. See Note F.

Although Ms. Plaza is responsible for the taxes on the Plaza's taxable income for the period from December 1, 2005 to January 24, 2006, pursuant to the Plaza Agreement, the Company agreed to reimburse Ms. Plaza for the income taxes applicable to said taxable income. The reimbursement amounts to \$125,227 and was paid on June 15, 2006.

Property and equipment

Owned property and equipment, and leasehold improvements are stated at cost. Equipment and vehicles under capital leases are stated at the lower of fair market value or net present value of the minimum lease payments at the inception of the leases.

Depreciation of owned assets, and amortization of assets under capital leases and leasehold improvements, are provided using the straight-line basis over the shorter of the estimated useful lives of the assets or the lease term. Major renewals and betterments that extend the life of the assets are capitalized, while expenditures for repairs and maintenance are expensed when incurred.

The Company evaluates for impairment its long-lived assets to be held and used, and long-lived assets to be disposed of, whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable.

Intangible assets

Definite-lived intangible assets, such as customer lists and covenants not to compete, are amortized on a straight-line basis over their estimated useful lives. The Company continually evaluates the reasonableness of the useful lives of these assets.

Stock-based compensation

Effective November 1, 2006, the Company adopted the provisions of SFAS No. 123R, "Share-Based Payment" ("SFAS 123R"), and Staff Accounting Bulletin No. 107 ("SAB 107") using the modified prospective method, which results in the provisions of SFAS 123R being applied to the consolidated financial statements on a prospective basis. Under the modified prospective recognition method, restatement of consolidated income from prior periods is not required, and accordingly, the Company has not provided such restatements. Under the modified prospective provisions of SFAS 123R, compensation expense is recorded for the unvested portion of previously granted awards that were outstanding on November 1, 2006 and all subsequent awards. SFAS 123R requires that all stock-based compensation expense be recognized in the financial statements based on the fair value of the awards. Stock-based compensation cost is measured at the grant date based on the fair value of the award and is recognized as expense over the requisite service

period, which generally represents the vesting period, and includes an estimate of awards that will be forfeited. The Company calculates the fair value of stock options using the Black-Scholes option-pricing model at grant date. SFAS 123R also amends SFAS No. 95, "Statement of Cash Flows", to require that excess tax benefits related to stock-based compensation be reflected as cash flows from financing activities rather than cash flows from operating activities. The Company does not recognize such cash flow from financing activities since there has been no tax benefit related to the stock-based compensation.

As required under the new standards, stock option compensation expense is based on the anticipated vesting of the options. Forfeitures estimated when recognizing compensation expense are adjusted when actual forfeitures differ from the estimate.

Income per Share of Common Stock

Basic income per share of common stock is calculated by dividing net income by the weighted average number of shares of common stock outstanding. Diluted income per share includes the dilution of common stock equivalents. Pursuant to reverse acquisition accounting treatment, the weighted average number of shares outstanding in the computation of basic income per share was derived by weighting (i) for the period prior to the reverse acquisition transaction, the 1,150,000 shares received by the former stockholder of Plaza and the 600,000 shares received by San Juan Holdings, Inc., and (ii) for the period after the transaction, the number of shares outstanding represented the outstanding shares of Pharma-Bio that are outstanding. Diluted income per share includes the dilution of common equivalents. Accordingly, the series A preferred stock was deemed outstanding from the date of issuance until April 25, 2006, when the Company's restated certificate of incorporation was filed with the Secretary of State of Delaware and the shares of series A preferred stock were automatically converted into common stock. The warrants were deemed to be outstanding from the date of issuance to the end of the reporting period, except for common stock purchase warrants issued to the investment banker for Plaza as a result of the reverse acquisition, which were deemed to be outstanding through all periods prior to the reverse acquisition.

The weighted average shares of common stock outstanding (basic and diluted) were calculated using the treasury stock method for the respective periods.

NOTE B - RECENT ACCOUNTING PRONOUNCEMENTS

1. In February 2007, the Financial Accounting Standards Board (FASB) issued Statement No. 159 "The Fair Value Option for Financial Assets and Financial Liabilities - Including an Amendment of FASB Statement No. 115". This Statement permits entities to choose to measure many financial instruments and certain other items at fair value. The objective is to improve financial reporting by providing entities with the opportunity to mitigate volatility in reported earnings caused by measuring related assets and liabilities differently without having to apply complex hedge accounting provisions. This Statement is expected to expand the use of fair value measurement, which is consistent with the FASB's long-term measurement objectives for accounting for financial instruments.

This Statement is effective as of the beginning of an entity's first fiscal year that begins after November 15, 2007. Early adoption is permitted as of the beginning of a fiscal year that begins on or before November 15, 2007, provided the entity also elects to apply the provisions of FASB Statement No. 157, "Fair Value Measurements".

Management does not expect that the application of this standard will have any significant effect on the Company's financial statements.

2. In September 2006, the FASB published Statement No. 157 “Fair Value Measurement”. This Statement defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles (GAAP), and expands disclosures about fair value measurements. This Statement applies under other accounting pronouncements that require or permit fair value measurements, the FASB having previously concluded in those accounting pronouncements that fair value is the relevant measurement attribute. Accordingly, this Statement does not require any new fair value measurements. However, for some entities, the application of this Statement will change current practice. The changes to current practice resulting from the application of this Statement relate to the definition of fair value, the methods used to measure fair value, and the expanded disclosures about fair value measurements.

This Statement is effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. Earlier application is encouraged, provided that the reporting entity has not yet issued financial statements for that fiscal year, including financial statements for an interim period within that fiscal year. The provisions of this Statement should be applied prospectively as of the beginning of the fiscal year in which this Statement is initially applied, except for certain exceptions stated in the Statement.

The implementation of this Statement will have no significant effect on the Company’s financial statements.

3. In June 2006, the FASB issued Interpretation No. 48 “Accounting for Uncertainty in Income Taxes—an interpretation of FASB Statement No. 109” (“FIN 48”). This Interpretation clarifies the accounting for uncertainty in income taxes recognized in an enterprise’s financial statements in accordance with FASB Statement No. 109, “Accounting for Income Taxes”. FIN 48 prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. This Interpretation also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure, and transition. This Interpretation is effective for fiscal years beginning after December 15, 2006. Earlier application of the provisions of this Interpretation is encouraged if the enterprise has not yet issued financial statements, including interim financial statements, in the period this Interpretation is adopted. Management does not expect that the application of this standard will have any significant effect on the Company’s results of operations or its financial condition.

4. Other recently issued FASB Statements or Interpretations, SEC Staff Accounting Bulletins, and AICPA Emerging Issue Task Force Consensuses have either been implemented or are not applicable to the Company.

NOTE C - CAPITAL TRANSACTIONS

On January 24, 2006, Pharma-Bio effected a two-for-one share distribution with respect to its common stock pursuant to which Pharma-Bio issued one share of common stock for each share outstanding on the record date, January 24, 2006. All share and per share information in these financial statements give retroactive effect to this share distribution.

On January 25, 2006, contemporaneously with the consummation of the acquisition, Pharma-Bio sold, in a private placement, 47 units, each unit consisting of 25,000 shares of series A preferred stock, warrants to purchase 85,100 shares of common stock at \$1.10 per share and warrants to purchase 85,100 shares of common stock at \$1.65 per share. In the private placement, Pharma-Bio issued an aggregate of 1,175,000 shares of series A preferred stock (which were convertible into an aggregate of 15,998,800 shares of common stock), warrants to purchase 3,999,700 shares of common stock at \$1.10 per share, and warrants to purchase 3,999,700 shares of common stock at \$1.65 per share, to 42 accredited investors. Pharma-Bio paid brokerage commissions of 10% of the gross purchase price and an aggregate non-accountable expense allowance of 3% of the gross purchase price with respect to the units sold. In certain cases, the broker waived the commission and non-accountable expense allowance, and the investor paid the purchase price less the commission and non-accountable expense allowance. The purchase price for the 47 units sold was \$11,750,000. Broker-dealers waived commission and non-accountable expense allowance with respect to \$628,750, Pharma-Bio paid commissions and non-accountable expense allowances totaling \$898,750, and

Pharma-Bio issued warrants to purchase an aggregate of 1,439,892 shares of common stock. The warrants have an exercise price of \$.7344 per share and a term of three years.

Each share of series A preferred stock automatically converted into 13.616 shares of common stock, or an aggregate of 15,998,800 shares of common stock, upon the filing, on April 25, 2006, of a restated certificate of incorporation which increased the authorized capital stock to 10,000,000 shares of preferred stock and 50,000,000 shares of common stock.

The subscription agreement pursuant to which the series A preferred stock and warrants were issued required Pharma-Bio to file a registration statement within 60 days after the effective date of the merger between Plaza and Plaza Acquisition Corp. The effective date of the merger was January 25, 2006, therefore, the 60-day term expired on March 26, 2006. Since Pharma-Bio failed to file the registration statement by that date, Pharma-Bio was required to issue .0003 shares of common stock for each share of common stock issued upon conversion of the series A preferred stock for each day of delay. Pharma-Bio was three days late, therefore, 14,401 shares of common stock were issued to the former holders of the series A preferred stock.

The warrants issued in the private placement expire five years from the closing date (January 25, 2011) and are callable by Pharma-Bio if the closing price of the common stock is at least twice the exercise price of the warrants for twenty (20) consecutive trading days.

In January 2004, Pharma-Bio issued warrants to purchase 800,000 shares of common stock at \$0.12 per share (1,600,000 shares at \$0.06 per share, subsequent to the stock distribution effected on January 24, 2006). The warrants may also be converted into shares of common stock on a cashless basis under certain conditions, but on a reduced number of shares. The warrants expire on January 16, 2014. In January 2007, warrants to purchase a total of 1,350,400 shares of common stock were converted to 1,300,539 shares of common stock pursuant to the cashless exercise provisions. As of April 30, 2007, warrants to purchase 249,600 shares remain outstanding.

NOTE D - PROPERTY & EQUIPMENT

The balance of property and equipment as of April 30, 2007 consists of:

	Useful life (years)	Amount
Vehicles	5	\$ 221,434
Computers	3	180,758
Equipment	3	120,505
Furniture and fixtures	10	68,509
Total		591,206
Less: Accumulated depreciation and amortization		(276,722)
Property and equipment, net		\$ 314,484

NOTE E - OTHER ASSETS

At April 30, 2007, non-current other assets include the following:

Intangible assets:

Covenant not to compete	\$ 71,667
Customer-related intangibles	83,333
Other assets	13,391
	\$ 168,391

Covenant not to compete represents the portion of the payment made in connection with the purchase of the Plaza stock that was allocated to a non-competition covenant. Under this agreement, the sole stockholder of Plaza agreed not to compete with the Company for a period of five years. This amount is amortized on the straight-line method over the five-year term of the non-competition covenant.

Customer-related intangible assets consist mainly of a customer list that Plaza acquired along with certain other assets from a business which performs in the United States consulting services similar to those performed by the Company in Puerto Rico. The value of the customer list is being amortized on the straight-line method over its estimated useful life of three years.

All of the intangible assets were originated in January 2006, therefore, there was no amortization of intangible assets in prior periods. The amortization expense for each of the three-month periods ended April 30, 2007 and 2006 amounted to \$17,500, and for the six-month periods ended April 30, 2007 and 2006 amounted to \$35,000 and \$25,000, respectively.

NOTE F - INCOME TAXES

The Company's taxable income is subject to the Puerto Rico income tax at the 20% to 39% rates provided by the 1994 Puerto Rico Internal Revenue Code, as amended. However, on August 1, 2005, Puerto Rico Act No. 41 was approved, which imposes an additional 2.5% special tax to all corporations and partnerships having a net taxable income over \$20,000. The Act was effective for taxable years commencing after December 31, 2004 and ending on or before December 31, 2006; however, on November 10, 2006, Puerto Rico Act No. 244 was approved to impose the additional 2.5% special tax to taxable years commencing after December 31, 2004 and before January 1, 2007. Therefore, the Company's maximum effective tax rate will be 41.5% for its fiscal years ending on October 31, 2006 and October 31, 2007, and 39% thereafter.

The operations carried out by the Company's subsidiary in the United States (which are presently not significant) are taxed in the United States. With certain limitations, the Company receives a credit on its Puerto Rico tax for the federal income tax paid. Also, upon distribution of earnings by the Puerto Rican subsidiary to its parent those dividends are taxed at the federal level, however, the parent is able to receive a credit for the taxes paid by the subsidiary on its operations in Puerto Rico, to the extent of the federal taxes that result from those earnings (determined at rates which are normally lower than in Puerto Rico). As a result, the income tax expense of the Company, under its present corporate structure, would normally be the Puerto Rico taxes on operations in said jurisdiction, plus 10% withholding in Puerto Rico from dividends paid to the Puerto Rican subsidiary's parent, plus federal taxes on operations in the United States.

The Company has not recognized deferred income taxes on \$1,067,445 of undistributed earnings of its Puerto Rican subsidiary, since such earnings are considered to be reinvested indefinitely. If the earnings were distributed in the form of dividends, the Company would be subject to a \$106,745 tollgate tax.

The income tax expense is computed at statutory rates applied to income calculated in accordance with the accounting practices described herein and as shown in the financial statements. Deferred income tax assets and liabilities are computed for differences between the financial statements and tax bases of assets and liabilities that will result in taxable or deductible amounts in the future, based on enacted tax laws and rates applicable to the periods in which the

differences are expected to affect taxable income.

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The reasons for the difference between the income tax expense applicable to income before income taxes and the amount computed by applying the statutory tax rate in Puerto Rico, were as follows:

	Three months ended April 30,		Six months ended April 30,	
	2007	2006	2007	2006
Theoretical income tax expense by application of statutory rates to the book pre-tax	\$ 375,184	\$ 362,527	\$ 618,113	\$ 742,437
Permanent differences:				
Effect of income subject to taxation under Subchapter N (taxable income taxed to stockholders)	-	-	-	(358,037)
Other permanent differences	10,561	35,778	23,587	35,778
Income tax expense	\$ 385,745	\$ 398,305	\$ 641,700	\$ 420,178

Because Plaza was treated as an N Corporation under the Puerto Rico Internal Revenue Code through January 24, 2006, its income was taxed to its stockholder through said date, and Plaza did not pay income tax. Had income tax been paid at the statutory rate, the Company's net income would have been \$1,010,790, or \$0.39 per share (basic) and \$0.07 per share (diluted), for the six months ended April 30, 2006.

NOTE G - RELATED PARTY TRANSACTIONS; DUE TO AFFILIATE

On January 25, 2006, pursuant to the Plaza Agreement, Elizabeth Plaza, as the sole stockholder of Plaza and affiliate of Plaza, received at the closing \$10,000,000 plus 1,150,000 shares of Pharma-Bio's common stock. In addition, the Company agreed to pay Ms. Plaza three payments of \$2,750,000, including imputed interest determined in accordance with Section 1274 of the Internal Revenue Code, on January 25, 2007, 2008, and 2009. However, in January 2007, Elizabeth Plaza agreed to accept the first installment of \$2,750,000 in two payments, one of \$2,500,000 in January 2007 and the second of \$250,000 in February 2007. The April 30, 2007 outstanding payments are due as follows:

Twelve months ending April 30,	Amount
2008	\$ 2,750,000
2009	2,750,000
Total payments	5,500,000
Less: imputed interest	(436,310)
Present value of total payments	5,063,690
Less: current portion	(2,613,225)
Long-term portion	\$ 2,450,465

As a condition to closing, Plaza was required to have a net tangible book value of not less than \$5,500,000, of which at least \$2,000,000 was in cash, as of November 30, 2005. Subject to the requirement that Plaza have at least \$2,000,000 in cash as of November 30, 2005, the purchase price was to be adjusted upward or downward depending on the net tangible book value, determined as provided in the Plaza agreement. This provision resulted in an additional payment to Ms. Plaza in the amount of \$88,161, which was paid during the third quarter of 2006.

The Plaza Agreement also provides that Plaza, rather than Ms. Plaza, is responsible for the income tax from December 1, 2005 through the closing date, which was January 25, 2006. Because of the status of Plaza as an N Corporation under the Puerto Rico Internal Revenue Code, Plaza's net income from December 1, 2005 to January 24, 2006 was taxed to Ms. Plaza. The income tax payable by Ms. Plaza for Plaza's taxable income for that period amounts to \$125,227. Plaza reimbursed Ms. Plaza the \$125,227 during the third quarter of 2006. The \$88,161 payment described in the preceding paragraph and the \$125,227 payment described in this paragraph are treated as additional payments on account of the purchase price of Plaza stock from Mrs. Plaza.

Pursuant to the Puerto Rico Internal Revenue Code, the Company's clients are required to withhold a percentage of its fees (usually 3%, but sometimes 7%) as withheld income tax and remit such amount to the Puerto Rico Department of the Treasury. Such payment is treated as a payment on account to the Company's income tax obligations. Prior to January 25, 2006, Plaza was an N Corporation, and the Company's taxable income was taxed to Ms. Plaza, as sole stockholder. Accordingly, such withheld taxes were treated as a distribution to Ms. Plaza, as the Company's sole stockholder, since Ms. Plaza was the person entitled to take the credit for the income tax withheld by the Company's clients in her personal income tax return. The amounts withheld prior to January 25, 2006 are recognized in the financial statements as non-cash distributions.

San Juan Holdings represented Plaza and Elizabeth Plaza in connection with the reverse acquisition. For such services, Pharma-Bio issued 600,000 shares of common stock and warrants to purchase 2,500,000 shares of common stock, with an exercise price of \$.06 per share, to San Juan Holdings. In Pharma-Bio's private placement of series A preferred stock and warrants, San Juan Holdings purchased three units. The purchase price for the three units was \$750,000. The broker, which is an affiliate of San Juan Holdings, waived the commission and non-accountable expense allowance with respect to such sales, and as a result, San Juan Holdings purchased the three units for a net payment of \$652,500. The Company also paid an affiliate of San Juan Holdings a broker's commission and non-accountable expense allowance of \$195,000 for sales made to other purchasers in the private placement, and Pharma-Bio issued to the affiliate three-year warrants to purchase an aggregate of 275,724 shares of common stock at an exercise price of \$.7344 per share.

NOTE H - COMMITMENTS

CONTRACTS

On January 25, 2006, the Company entered into employment agreements with Elizabeth Plaza and Nelida Plaza. The agreement with Elizabeth Plaza initially provided that Ms. Plaza will serve as president and chief executive officer of the Company for a period of 18 months, for which she will receive a salary at the annual rate of \$250,000. For 18 months thereafter, Ms. Plaza will serve as a consultant for which she will receive compensation at the annual rate of \$75,000. During the term of her employment, the Company will also provide Ms. Plaza with an automobile allowance at the annual rate of \$24,828, discretionary bonuses and stock options or other equity-based incentives as shall be determined by the compensation committee's board of directors, except that her bonus shall not be less than 4% nor more than 50% of her salary. If the Company terminates Ms. Plaza's employment other than for cause or as a result of her death or disability, the Company is required to pay Ms. Plaza the balance of her compensation for her employment terms and her consulting term and other benefits, including a pro rata portion of the bonus that would have been paid to her, and her obligations under her non-competition provision terminate. In January 2007, Elizabeth Plaza's employment agreement was amended to extend her employment term through December 31, 2007, and the consulting term will immediately commence following the employment term and end on January 31, 2009.

The Company's agreement with Nélide Plaza provides that Ms. Plaza will serve as vice president for a term of three years for which she will receive annual compensation at the annual rate of \$150,000. She is also entitled to such bonus compensation as is determined by the compensation committee, not to exceed 50% of her salary. The Company also agreed to make the lease payments on the automobile she currently leases. Such payments are at the annual rate of approximately \$11,600. If the Company terminates Ms. Plaza's employment other than for cause or as a result of her death or disability, the Company is required to pay Ms. Plaza the balance of her compensation for her employment terms and her consulting term and other benefits, including a pro rata portion of the bonus that would have been paid to her, and her obligations under her non-competition provision, terminate.

Lease commitments

Capitalized lease obligations -As of April 30, 2007, the Company leases vehicles under non-cancelable capital leases with a cost of \$221,434 (accumulated depreciation of \$77,932). Depreciation expense for these assets amounted to \$11,072 and \$11,589 in the three-month periods ended April 30, 2007 and 2006, respectively. The following is a schedule, by year, of future minimum lease payments under the capitalized leases together with the present value of the net minimum lease payments at April 30, 2007:

Twelve months ending April 30,	Amount
2008	\$ 48,240
2009	48,240
2010	69,974
2011	9,385
Total minimum lease payments	175,839
Less: Amount of imputed interest	(14,366)
Present value of minimum lease payments	161,473
Current portion of obligation under capital leases	(40,430)
Long-term portion	\$ 121,043

Operating facilities - The Company conducts its administrative operations in office facilities which are leased under three different rental agreements with the following terms:

Description	Monthly Rent	Commitment Term
Headquarter offices and laboratory testing facilities	\$ 18,750	Ending in January 2012, with one five year renewal option
Housing for employees	\$ 1,850	On a month to month basis
Limerick office space	\$ 1,000	Ending in July 2007

The first lease listed in the table is with an affiliate of the chief executive officer. In February 2007, the Company and the affiliate rescinded a former lease agreement and entered into a new agreement. The monthly payments under the new lease agreement, which amount to \$18,750, will increase by 5% annually. The new agreement also requires the payment of utilities, property taxes, insurance and a portion of expenses incurred by the affiliate in connection with the maintenance of common areas. The Company paid a monthly rental of \$3,200 under the lease agreement of its former main resources facilities.

In June 2006, the Company entered into a lease agreement for office facilities in Limerick, Pennsylvania, at a monthly rental of \$1,000. The lease term expires on July 31, 2007. The lease agreement may be renewed for an additional term of three years at monthly rental of \$1,050 during the first year, \$1,100 during the second year, and \$1,150 during the third year of the lease renewal term.

Rent expense during the three-month periods ended April 30, 2007 and 2006 amounted to \$70,913 and \$26,400, respectively, and \$89,063 and \$52,700 for the six-month period ended April 30, 2007 and 2006, respectively.

NOTE I - STOCK OPTIONS AND STOCK-BASED COMPENSATION

In October 2005, the Company's board of directors adopted, and on April 25, 2006, the Company's stockholders approved, the 2005 Long-Term Incentive Plan, covering 2,500,000 shares of common stock. The 2005 plan provides for the grant of incentive and non-qualified options, stock grants, stock appreciation rights and other equity-based incentives to employees, including officers, and consultants. The 2005 plan is to be administered by a committee of independent directors. In the absence of a committee, the plan is administered by the board of directors. Independent directors are not eligible for discretionary options. However, each newly elected independent director receives at the time of his or her election, a five-year option to purchase 25,000 shares of common stock at the market price on the date of his or her election. In addition, the plan provided for the annual grant of an option to purchase 5,000 shares of common stock on the first trading day of January of each year, commencing January 2007; however, on April 19, 2007, the stockholders amended the plan to increase the number of options granted to its independent directors annually from 5,000 to 10,000 shares of common stock. On April 19, 2007, the stockholders also amended the plan to provide for a grant to purchase 5,000 shares of common stock at the market price to each advisory board member on the date of his or her election and a grant of 5,000 options to each of them annually. The options to directors have a term of five years and become exercisable cumulatively as to 50% of the shares subject to the option six months from the date of grant and, as to the remaining 50%, 18 months from the date of grant. Pursuant to these provisions, the Company has granted options to purchase 25,000 shares at \$0.7344 per share and 5,000 shares at \$0.75 to each of the three independent directors. Options intended to be incentive stock options must be granted at an exercise price per share which is not less than the fair market value of the common stock on the date of grant and may have a term which is not longer than ten years. If the option holder holds at least 10% of our common stock, the exercise price must be at least 110% of the fair market value on the date of grant and the term of the option cannot exceed five years.

Pursuant to the Plaza Agreement, all outstanding options issued by Plaza were terminated, and the Company granted incentive stock options to purchase an aggregate of 1,400,000 shares of common stock at an exercise price of \$0.7344 per share to the holders of such terminated Plaza options pursuant to the Company's 2005 Long-Term Incentive Plan. Of the total options to purchase 1,400,000 shares of common stock, options to purchase 776,186 shares of common stock were granted to 18 employees whose options to purchase Plaza common stock were cancelled. The options to purchase the remaining 623,814 shares of common stock were granted to both the 18 former holders of Plaza options and 23 additional Plaza employees. The Company subsequently granted options to purchase other 648,724 shares to employees, independent directors and an independent contractor. The new options have a weighted average exercise price of approximately \$0.76, a term of five years and are exercisable in installments. As of April 30, 2007, there were approximately outstanding options to purchase 1,429,519 shares of common stock, since some options expired because of employment terminations.

The following table presents the stock-based compensation included in the Company's consolidated statement of income and the effect on earnings per share:

	Three months ended April 30, 2007	Six months ended April 30, 2007
Stock-based compensation expense:		
Cost of services	\$ 10,184	\$ 42,090
Selling, general and administrative	16,168	23,284
Stock-based compensation before tax	26,352	65,374

Income tax benefit		—		—
Net stock-based compensation expense	\$	26,352	\$	65,374
Effect on earnings per share:				
Basic earnings per share	\$	(0.001)	\$	(0.003)
Diluted earnings per share	\$	(0.001)	\$	(0.003)

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Prior to the adoption of SFAS 123R and SAB 107, the Company followed APB 25, and compensation cost related to employee stock options was generally not recognized because options were granted with exercise prices equal to or greater than the fair market value at the date of grant. Had compensation cost for the stock option plans been determined based on the fair value at the grant date for awards in the three-month and six-month periods ended April 30, 2006, consistent with the provisions of SFAS No. 123R, the effect on Company's net income and earnings per share would not have been significant.

The fair value of each stock option granted prior to November 1, 2006 was estimated at \$0.60 by the Company's investment bankers based on its valuation given that the Company's stock had not yet traded and given that the value of the options cannot exceed the market price of the common stock (\$0.7344) in the most recent issuance of securities by the Company, which was its January 2006 private placement.

The fair value of each stock option granted on or after November 1, 2006 was estimated on the date of grant using the Black-Scholes option pricing model using the following weighted average assumptions (expected volatility is based upon the historical volatility of the Company's stock price):

Expected dividend yield	0.0%
Expected stock price volatility	10%
Risk free interest rate	4.7%
Expected life of options	2.65 years

Weighted average fair value per share of options granted during the six-month period ended April 30, 2007	\$ 0.1506
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As of November 1, 2006 there were outstanding options to acquire 1,348,090 shares of common stock. During the three month period ended January 31, 2007, the Company granted options to purchase 5,000 shares of common stock to each of its three independent directors and an option to purchase 50,000 shares to its new general manager. No options were exercised or expired during the six-month period ended April 30, 2007. Therefore, as of April 30, 2007, there were outstanding options to purchase 1,413,909 shares. The weighted average of the remaining contractual life of the outstanding stock options is 4 years and the weighted average exercise price is \$0.7467.

Pursuant to the Plaza Agreement, Pharma-Bio agreed that it would issue 100 shares of common stock to each of Plaza's eligible employees. Such shares will not be issued until Pharma-Bio files a Form S-8 registration statement in connection with the issuance of such shares. Approximately 16,500 shares of common stock may be issued pursuant to this program.

NOTE J - CONCENTRATION OF RISKS

The Company's cash balances are maintained in a bank checking account and a money market account.

Management deems all its accounts receivables to be fully collectible, and, as such, does not maintain any allowances for uncollectible receivables.

The Company's revenues, and the related receivables, are concentrated in the pharmaceutical industry in Puerto Rico. A small number of customers have accounted for a significant percentage of its revenue. In spite of the fact that just a few customers represent a significant source of revenue, the Company's functions are not a continuous process, accordingly, the client base for which the Company's services are typically rendered, on a project-by-project basis, changes regularly. The following table sets forth information as to revenues (dollars in thousands) and percentage of revenues for the Company's principal clients, all of which are pharmaceutical companies:

Customer	Three months ended April 30,		Six months ended April 30,	
	2007	2006	2007	2006
GlaxoSmithKline	\$ 1,102 (26.4%)	\$ 1,166 (30.6%)		