

Pharma-Bio Serv, Inc.  
Form 10-Q  
March 17, 2009

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

FORM 10-Q

(Mark One)

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

For the quarterly period ended January 31, 2009

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.  
(Exact Name of Registrant as Specified in Its Charter)

Delaware  
(State or Other Jurisdiction of  
Incorporation or Organization)

20-0653570  
(IRS Employer  
Identification No.)

Pharma-Bio Serv Building,  
Industrial Zone Lot 14, Barrio Higuillar,  
Dorado, Puerto Rico  
(Address of Principal Executive Offices)

00646  
(Zip Code)

Registrant's Telephone Number, Including Area Code 787-278-2709

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or 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 large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer   
Non-accelerated filer

Accelerated filer   
Smaller reporting company

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

The number of shares of the registrant's common stock outstanding as of March 15, 2009 was 20,751,215.



PHARMA-BIO SERV, INC.  
FORM 10-Q  
FOR THE QUARTER ENDED JANUARY 31, 2009

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## PART I – FINANCIAL INFORMATION

Item 1.

## FINANCIAL STATEMENTS

PHARMA-BIO SERV, INC.  
Condensed Consolidated Balance Sheets  
(Unaudited)

	January 31, 2009	October 31, 2008
<b>ASSETS:</b>		
Current assets		
Cash and cash equivalents	\$ 1,564,897	\$ 3,087,990
Accounts receivable	2,254,447	3,245,153
Other	236,046	194,108
Total current assets	4,055,390	6,527,251
Property and equipment		
Other assets	142,706	63,127
Total assets	\$ 5,708,973	\$ 8,111,953
<b>LIABILITIES AND STOCKHOLDERS' EQUITY:</b>		
Current liabilities		
Current portion-obligations under capital leases	\$ 58,239	\$ 45,318
Accounts payable and accrued expenses	1,009,902	1,189,705
Due to affiliate	500,000	2,706,892
Income taxes payable	7,664	48,324
Total current liabilities	1,575,805	3,990,239
Other long-term liabilities		
Total liabilities	1,621,784	4,060,173
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 20,751,215 shares	2,075	2,075
Additional paid-in capital	558,113	540,337
Retained earnings	3,553,506	3,534,060
Accumulated other comprehensive loss	(26,505)	(24,692)
Total stockholders' equity	4,087,189	4,051,780
Total liabilities and stockholders' equity	\$ 5,708,973	\$ 8,111,953

See notes to condensed consolidated financial statements.

PHARMA-BIO SERV, INC.  
Condensed Consolidated Statements of Income  
(Unaudited)

	Three months ended January 31,	
	2009	2008
REVENUES	\$ 2,893,516	\$ 3,604,303
COST OF SERVICES	2,031,782	2,241,882
GROSS PROFIT	861,734	1,362,421
SELLING, GENERAL AND ADMINISTRATIVE EXPENSES	711,916	815,910
INCOME FROM OPERATIONS	149,818	546,511
OTHER INCOME (EXPENSES):		
Interest expense	(44,616)	(88,110)
Interest income	11,095	43,415
Gain on disposition of property and equipment	7,950	-
	(25,571)	(44,695)
INCOME BEFORE INCOME TAXES	124,247	501,816
INCOME TAXES	104,801	219,093
NET INCOME	\$ 19,446	\$ 282,723
BASIC EARNINGS PER COMMON SHARE	\$ 0.009	\$ 0.014
DILUTED EARNINGS PER COMMON SHARE	\$ 0.009	\$ 0.013
WEIGHTED AVERAGE NUMBER OF COMMON SHARES OUTSTANDING – BASIC	20,751,215	19,615,539
WEIGHTED AVERAGE NUMBER OF COMMON SHARES OUTSTANDING – DILUTED	22,554,394	22,121,341

See notes to condensed consolidated financial statements.

PHARMA-BIO SERV, INC.  
Condensed Consolidated Statements of Cash Flows  
(Unaudited)

	Three months ended January 31,	
	2009	2008
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>		
Net income	\$ 19,446	\$ 282,723
Adjustments to reconcile net income to net cash provided by operating activities:		
Gain on disposition of property and equipment	(7,950)	-
Stock-based compensation	17,777	33,313
Depreciation and amortization	92,665	50,427
Imputed interest expense	43,108	86,255
Decrease in accounts receivable	1,033,921	400,228
(Increase) decrease in other assets	(40,333)	54,208
(Decrease) increase in liabilities	(223,486)	107,328
<b>NET CASH PROVIDED BY OPERATING ACTIVITIES</b>	<b>935,148</b>	<b>1,014,482</b>
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>		
Acquisition of property and equipment	(58,118)	(444,042)
Payments for business assets acquisition	(150,394)	-
Proceeds from sale of property and equipment	12,400	-
<b>NET CASH USED IN INVESTING ACTIVITIES</b>	<b>(196,112)</b>	<b>(444,042)</b>
<b>CASH FLOW FROM FINANCING ACTIVITIES:</b>		
Payments on obligations under capital lease	(11,034)	(10,205)
Payments to affiliate	(2,250,000)	-
<b>NET CASH USED IN FINANCING ACTIVITIES</b>	<b>(2,261,034)</b>	<b>(10,205)</b>
EFFECT OF EXCHANGE RATE CHANGES ON CASH	(1,095)	-
<b>NET (DECREASE) INCREASE IN CASH AND CASH EQUIVALENTS</b>	<b>(1,523,093)</b>	<b>560,235</b>
<b>CASH AND CASH EQUIVALENTS - BEGINNING OF PERIOD</b>	<b>3,087,990</b>	<b>4,792,366</b>
<b>CASH AND CASH EQUIVALENTS – END OF PERIOD</b>	<b>\$ 1,564,897</b>	<b>\$ 5,352,601</b>
<b>SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:</b>		
Cash paid during the period for:		
Income taxes	\$ 190,007	\$ -
Interest	\$ 1,507	\$ 1,855
<b>SUPPLEMENTARY SCHEDULES OF NON-CASH INVESTING AND FINANCING ACTIVITIES:</b>		
Accounts payable incurred in projects in process	\$ -	\$ 84,306
Income tax withheld by clients to be used as a credit in the Company's income tax return	\$ 4,013	\$ -
	\$ 31,995	\$ -

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Property and equipment disposed with an accumulated depreciation of  
\$27,544

Obligations under capital lease incurred for the acquisition of a vehicle	\$	-	\$	33,695
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See notes to condensed consolidated financial statements.

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PHARMA-BIO SERV, INC.  
Notes To Condensed Consolidated Financial Statements  
January 31, 2009  
(Unaudited)

NOTE A - ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

ORGANIZATION

Pharma-Bio Serv, Inc. (“Pharma-Bio”) is a Delaware corporation organized on January 14, 2004. Pharma-Bio is the parent company of Pharma-Bio Serv PR, Inc. (“Pharma-PR”), a Puerto Rico corporation, Pharma-Bio Serv US, Inc. (“Pharma-US”), a Delaware corporation, and Pharma-Bio Serv Validation & Compliance Limited (“Pharma-IR”), a majority owned Irish corporation. Pharma-Bio, Pharma-PR, Pharma-US and Pharma-IR are collectively referred to as the “Company.” The Company operates in Puerto Rico, the United States and in Ireland under the name of Pharma-Bio Serv and is engaged in providing technical compliance consulting services primarily to the pharmaceutical, chemical, medical device and biotechnology industries.

Pharma-US is a wholly owned subsidiary, which was organized in Delaware in July 2008. As of January 31, 2009, this subsidiary was in development stage and has not incurred significant revenues or expenses.

SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The condensed consolidated balance sheet of the Company as of October 31, 2008 is derived from audited consolidated financial statements but does not include all disclosures required by generally accepted accounting principles. The unaudited interim condensed consolidated financial statements, include all adjustments, consisting of normal recurring adjustments, which are, in the opinion of management, necessary for a fair presentation of the financial position and results of operations and cash flows for the interim periods. The results of operations for the three months ended January 31, 2009 are not necessarily indicative of expected results for the full 2009 fiscal year.

The accompanying financial data as of January 31, 2009, and for the three months ended January 31, 2009 and 2008 has been prepared by us, without audit, pursuant to the rules and regulations of the Securities and Exchange Commission (SEC). Certain information and footnote disclosures normally contained in financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted. These condensed consolidated financial statements should be read in conjunction with the financial statements and notes contained in our audited Consolidated Financial Statements and the notes thereto for the fiscal year ended October 31, 2008.

Consolidation

The accompanying condensed consolidated financial statements include the accounts of the Company and all of its wholly owned and majority-owned subsidiaries. All intercompany transactions and balances have been eliminated in consolidation.

Use of Estimates

The preparation of consolidated 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 consolidated financial statements and the reported amounts of revenues and expenses during the reporting periods. Actual results may 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 and cash equivalents, accounts receivable, accounts payable and accrued liabilities, are considered reasonable estimates of fair value due to their liquidity or short-term nature. Management believes, based on current rates, that the fair value of its obligations under capital leases and amounts due to affiliate approximates 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 (representing approximately 10% of total revenues), which revenue is recognized similarly, except that certain milestones also have to be reached before revenue is recognized. 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 Equivalents

For purposes of the consolidated statements of cash flows, cash equivalents include investments in a money market obligations trust that is registered under the U.S. Investment Company Act of 1940 and 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.

### 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 and amortization of owned assets are provided for, when placed in service, in amount sufficient to relate the cost of depreciable assets to operations over their estimated service lives, using straight-line basis. Assets under

capital leases and leasehold improvements are amortized, over the shorter of the estimated useful lives of the assets or initial 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. As of January 31, 2009 and October 31, 2008 the accumulated depreciation and amortization amounted to \$531,873 and \$480,085, respectively.

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. Based on management estimates, no impairment of the operating properties was present.

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#### 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

SFAS 123R requires that all stock-based compensation expense be recognized in the consolidated 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.

#### Income Per Share of Common Stock

Basic income per share of common stock is calculated 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.

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

#### Foreign Operations

The functional currency of the Company's foreign subsidiary is its local currency. The assets and liabilities of the Company's foreign subsidiary are translated into U.S. dollars at exchange rates in effect at the balance sheet date. Income and expense items are translated at the average exchange rates prevailing during the period. The cumulative translation effect for subsidiaries using a functional currency other than the U.S. dollar is included as a cumulative translation adjustment in stockholders' equity and as a component of comprehensive income.

The Company's intercompany accounts are typically denominated in the functional currency of the foreign subsidiary. Gains and losses resulting from the remeasurement of intercompany receivables that the Company considers to be of a long-term investment nature are recorded as a cumulative translation adjustment in stockholders' equity and as a component of comprehensive income, while gains and losses resulting from the remeasurement of intercompany receivables from those international subsidiaries for which the Company anticipates settlement in the foreseeable future are recorded in the consolidated statements of operations. The net gains and losses recorded in the consolidated statements of income were not significant for the periods presented.

#### Reclassifications

Certain reclassifications have been made to the January 31, 2008 condensed consolidated financial statements to conform them to the January 31, 2009 condensed consolidated financial statements presentation. Such reclassifications do not have effect on net income as previously reported.



## NOTE B - RECENT ACCOUNTING PRONOUNCEMENTS

1. In December 2007, the Financial Accounting Standards Board (FASB) issued SFAS No. 141R, Business Combinations (“SFAS 141R”). SFAS 141R requires: the assets acquired and liabilities assumed to be measured at fair value as of the acquisition date; liabilities related to contingent consideration to be remeasured at fair value at each subsequent reporting period; and acquisition-related costs to be expensed as these are incurred. SFAS 141R also requires additional disclosures of information surrounding a business combination. The provisions of SFAS 141R are effective for fiscal years beginning on or after December 15, 2008 and apply to business combinations that are completed on or after the date of adoption. The Company has not yet adopted this pronouncement, but expects that the nature and magnitude of the specific effects will depend upon the nature, terms and size of the acquisitions the Company completes after the effective date, if any.

2. In December 2007, the FASB issued Statement No. 160 “Noncontrolling Interests in Consolidated Financial Statements - an amendment of ARB No. 51”. This Statement applies to all entities that prepare consolidated financial statements, but will affect only those entities that have an outstanding noncontrolling interest in one or more subsidiaries or that deconsolidate a subsidiary. This statement is effective for fiscal years, and interim periods within those fiscal years, beginning on or after December 15, 2008. Earlier adoption is prohibited.

3. In February 2007, the 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. The application of this standard had no significant effect on the Company’s consolidated financial statements.

4. In September 2006, the FASB issued 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. 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 application of this standard had no significant effect on the Company’s consolidated financial statements.

5. 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 - INCOME TAXES

On July 2008, Pharma-Bio and Pharma-PR obtained a Grant of Industrial Tax Exemption (“the Grant”) from the Puerto Rico Industrial Development Company pursuant to the terms and conditions set forth in Act No. 135 of December 2, 1997, as amended. The Grant provides relief on various Puerto Rico taxes, including income tax, mostly for the

Company's new microbiological testing facility and service activities outside of Puerto Rico. The Grant is effective as of September 1, 2007 and covers a ten year period. Activities covered by the Grant are subject to a reduced income tax rate of 7%.

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The operations carried out in the United States by the Company's subsidiary 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 Puerto Rico, 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.

Deferred income tax assets and liabilities are computed for differences between the consolidated 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.

The Company has not recognized deferred income taxes on 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 tollgate tax.

Pharma-Bio, Pharma-IR and Pharma-PR have unused operating losses which result in a potential deferred tax asset. However, an allowance has been provided covering the total amount of such balance since it is uncertain whether the net operating losses can be used to offset future taxable income before their expiration dates. Realization of future tax benefits related to a deferred tax asset is dependent on many factors, including the company's ability to generate taxable income. Accordingly, the income tax benefit will be recognized when realization is determined to be more probable than not. These net operating losses are available to offset future taxable income and expire for Pharma-Bio and Pharma-PR in 2026 and 2015, respectively, while for Pharma-IR are available indefinitely.

The statutory income tax rate differs to the effective rate mainly due to the new tax activities in Ireland and our microbiological testing facility which don't have previous taxable income where their current net operating losses could be carried back and derive a tax benefit. As previously mentioned, it is company policy to recognize tax benefits of net operating loss carryforwards when realization is determined to be more probable than not.

The Company adopted the provisions of FIN 48 which includes a two-step approach to recognizing, de-recognizing and measuring uncertain tax positions accounted for in accordance with SFAS 109. As of January 31, 2009, the Company had no significant uncertain tax positions that would be reduced as a result of a lapse of the applicable statute of limitations.

The Company files income tax returns in the U.S. in federal and various states jurisdictions, Puerto Rico and Ireland. The 2003 through 2008 tax years are open and may be subject to potential examination in one or more jurisdictions. We are not currently under federal, state, Puerto Rico or foreign income tax examination.

#### NOTE D - DUE TO AFFILIATE

Pursuant to a plan and agreement of merger dated January 25, 2006, the Company agreed to pay its then sole stockholder of Pharma-PR three installments of \$2,750,000 on January 25, 2007, 2008 and 2009, including imputed interest of 6.72%. In January 2009, the Company made an advance payment of \$2,250,000 over the final installment due on January 25, 2009. The Company expects to pay the remaining balance during fiscal year 2009. As of January 31, 2009 and October 31, 2008 the outstanding installment balances were:

	January 31, 2009	October 31, 2008
Amount due within the year ended October 31, 2009	\$ 500,000	\$ 2,750,000



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Less imputed interest	-	(43,108)
Present value of amount due	500,000	2,706,892
Current portion	(500,000)	(2,706,892)
Long-term portion	\$ -	\$ -

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## NOTE E – WARRANTS

At January 31, 2009 and October 31, 2008 the Company had outstanding warrants to purchase 11,053,216 and 12,188,892 shares, respectively, of the Company's common stock at prices ranging from \$0.06 to \$1.65 per share. The warrants became exercisable at various dates commencing in 2004 and expire at various dates through 2014.

On January 23, 2009, the Board of Directors of the Company authorized a one year extension on the expiration date of the outstanding warrants issued pursuant to, and subject to the terms and conditions of, those certain Series C Common Stock Purchase Warrants of the Company, dated as of January 25, 2006, and which were set to expire on January 24, 2009. In total, this extension of the expiration date of the common stock purchase warrants identified above will apply to an aggregate of 973,225 warrants. These warrants have an exercise price of \$0.7344.

## NOTE F – EARNINGS PER SHARE

The following data shows the amounts used in the calculations of basic and diluted earnings per share.

	Three months ended January 31,	
	2009	2008
Net income available to common equity holders - used to compute basic and diluted earnings per share	\$ 19,446	\$ 280,723
Weighted average number of common shares - used to compute basic earnings per share	20,751,215	19,615,539
Effect of warrants to purchase common stock	1,803,179	2,500,936
Effect of options to purchase common stock	-	4,866
Weighted average number of shares - used to compute diluted earnings per share	22,554,394	22,121,341

Warrants for the purchase of 8,972,625 and 9,687,956 shares of common stock for the three month periods ended in January 31, 2009 and 2008, respectively, were not included in computing diluted earnings per share because their effects were antidilutive. In addition, options for the purchase of 1,426,944 and 1,481,906 shares of common stock for the years ended in January 31, 2009 and 2008, respectively, were not included in computing diluted earnings per share because their effects were also antidilutive.

## NOTE G - CONCENTRATION OF RISKS

## Cash and cash equivalents

The Company maintains cash deposits in an FDIC insured bank and in a money market obligations trust, registered under the US Investment Company Act of 1940, as amended. The bank deposit balances frequently exceed federally insured limits. The money market fund is insured until April 30, 2009 under the United States Treasury Temporary Guarantee Program. No losses have been experienced or are expected on these accounts.

## Accounts receivable and revenues

Management deems all its accounts receivable 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, the United States of America and Ireland. Although few customers represent a significant source of revenue, the Company's functions are not a continuous process, accordingly, the client base for which the services are typically rendered, on a project-by-project basis, changes regularly.

The Company provided a substantial portion of its services to four customers, who accounted for 10% or more of its revenues in either of the three month periods ended January 31, 2009 or 2008. During the three months ended January 31, 2009 revenues from these customers were 29%, 23%, 12% and 7%, or a total of 71%, as compared to the same period last year for 27%, 25%, 5% and 13%, or a total of 70%, respectively. At January 31, 2009 amounts due from these customers represented 61% of total accounts receivable balance.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS.

The following discussion of our results of operations and financial condition should be read in conjunction with the financial statements and the related notes included under Part I Item 1 of this Quarterly Report on Form 10-Q. In addition, reference should be made to our audited Consolidated Financial Statements and notes thereto and related Management's Discussion and Analysis appearing in our Annual Report on Form 10-K for the year ended October 31, 2008. The following discussion includes forward-looking statements. For a discussion of important factors that could cause actual results to differ from results discussed in the forward-looking statements, see "Forward Looking Statements" below and the "Risk Factors" section in our Annual Report on Form 10-K for the year ended October 31, 2008.

Overview

We are a compliance services consulting firm with headquarters in Puerto Rico, servicing the Puerto Rico, United States and Europe markets. The compliance consulting service sector in those markets consists of local compliance and validation consulting firms, United States dedicated validation and compliance consulting firms and large publicly traded and private domestic and foreign engineering and consulting firms. We provide a broad range of compliance related consulting services. We market our services to pharmaceutical, chemical, biotechnology and medical devices, and allied products companies in Puerto Rico, the United States and Europe. Our staff includes more than 125 experienced engineering and life science professionals, and includes former quality assurance managers or directors, and experienced and trained professionals with bachelors, masters and doctorate degrees in health sciences and engineering.

We expanded the markets we serve from Puerto Rico to the United States and Ireland. We have offices in the United States and Ireland markets since fiscal years 2006 and 2008, respectively. The recently established Ireland operation, with an Ireland based management team reporting to our headquarters, has established a network of potential key customers and contacts that serve as the base for our sales target and opportunities.

We have plans to further penetrate the markets we currently serve. We will be marketing our services with an active presence in industry trade shows, professional conventions, industry publications and company provided seminars to the industry. Our senior management is also actively involved in the marketing process, especially in marketing to major accounts. Our senior management and staff also concentrate on developing new business opportunities and focus on the larger customer accounts (by number of professionals or dollar volume) and responding to prospective customers' requests for proposals.

While our core business is FDA and International agencies regulatory compliance related services we feel that our clients are in need of other services that we can provide and allow us to present the company as a global solution provider with a portfolio of integrated services that will bring value added solutions to our customers. Accordingly, in fiscal year 2009 we have expanded our portfolio of services to include a microbiological testing laboratory, an information technology consulting practice and an organically developed training center that will provide seminars/trainings to the industry.

Our new microbiological laboratory ("Lab") located in Puerto Rico, with an investment of \$1.3 million, incorporates the latest technology and test methodologies meeting pharmacopoeia industry standards and regulations. The Lab offers microbiological testing and related services to our core industries already serviced as well as the cosmetic and food industries.

During 2008, we identified the industry need, and the opportunity to provide, technical seminars/trainings that will incorporate the latest regulatory trends and standards as well as other related areas. A network of leading industry professional experts in their field, which includes resources of our own, were identified and teamed to provide these seminars/trainings to the industry. Our goal is to provide these services and market our company in the markets we currently serve as well as others.

In December 2008, we acquired the operations and assets of Integratek Corp. (“Integratek”), an information technology services and consulting firm based in Puerto Rico. Integratek provides a variety of information technology services such as web pages and portals development, digital art design, intranets, extranets, software development including database integration, Windows and web applications development, software technical training and learning management systems, technology project management, and compliance consulting services, among others. Integratek is a Microsoft Certified Partner and a reseller for technology products from leading vendors in the market. Although this acquired operation is currently small, our goal is to broaden the portfolio of services that we can provide to our customer base and also target other potential customers in other industries.

In line with the strategy to penetrate the United States market, we applied and on July 1, 2008 received certification as a "minority-controlled company" as defined by the National Minority Supplier Development Council and Growth Initiative ("NMSDC"). The certification will allow us to participate in corporate diversity programs available from various potential customers in the United States and Puerto Rico. The certification is subject to renewal on July 1, 2009.

On July 2008, Pharma-Bio and Pharma-PR obtained a Grant of Industrial Tax Exemption (“the Grant”) from the Puerto Rico Industrial Development Company pursuant to the terms and conditions set forth in Act No. 135 of December 2, 1997, as amended. The Grant provides relief on various Puerto Rico taxes, including income tax, mostly for our new Lab and service activities outside of Puerto Rico. The Grant is effective as of September 1, 2007 and covers a ten year period. Activities covered by the Grant are subject to a reduced income tax rate of 7%.

Although we believe we have instituted the right strategies to be profitable and seek growth, we cannot control the fact that the industry and the local and global economies are undergoing a recession and that has affected our operation and business growth.

The global economy recession and the industry worldwide consolidation continue to affect our fiscal year 2009 revenues and our growth plans. For the three months period ended in January 31, 2009 our total net revenues decreased by approximately \$0.7 million or 19.7%, when compared to the same period last year. In order to maintain volume in the markets we serve and ensure we are price competitive, we have adjusted our pricing and gross margin structure accordingly. In addition, we implemented cost containment measures and are refocusing the overall operations strategy to reduce its overhead costs. These factors have lead our net income for the three months period ended January 31, 2009 to be approximately \$19,000, a decline of \$264,000 or a reduction in profit margin of 7.1 percentage points when compared to the same period last year.

The following table sets forth information as to our revenue for the three months ended January 31, 2009 and 2008, by geographic regions (dollars in thousands).

Revenues by Region	Three months ended January 31,			
	2009		2008	
Puerto Rico	\$ 2,143	74.1%	\$ 2,724	75.6%
United States	601	20.8%	880	24.4%
Ireland	149	5.1%	-	-
	\$ 2,893	100.0%	\$ 3,604	100.0%

We believe our fiscal year 2009 profitability and liquidity is going to be highly dependent of the effect the global economy and worldwide industry consolidations will have over our operations, and our ability to seek service opportunities and adapt to the current industry trends.





## Results of Operations

The following table sets forth our statements of operations for the three-month periods ended January 31, 2009 and 2008, (dollars in thousands) and as a percentage of revenue:

	Three months ended January 31,			
	2009		2008	
Revenues	\$ 2,894	100.0%	\$ 3,604	100.0%
Cost of services	2,032	70.2%	2,242	62.2%
Gross profit	862	29.8%	1,362	37.8%
Selling, general and administrative costs	712	24.6%	816	22.7%
Interest expense	45	1.6%	88	2.4%
Interest income	11	-0.4%	44	-1.2%
Gain on disposition of property	8	-0.3%	-	0.0%
Income before income taxes	124	4.3%	502	13.9%
Income tax expense	105	3.6%	219	6.1%
Net income	19	0.7%	283	7.8%

Revenues. Revenues for the three months ended January 31, 2009 were \$2.9 million, a decrease of approximately \$0.7 million or 19.7%, when compared to the same period last year. The reduction is mainly attributable to the decrease of approximately \$0.5 million and \$0.3 million in the Puerto Rico and the United States market service revenue, respectively, partially offset by \$0.1 million generated by the Ireland operation.

Decreases in the service revenue are mostly due to the global economy recession and the closing of, or decrease in, operations of some pharmaceutical plants, triggered by operations consolidation.

Cost of Services; gross margin. For the three months ended January 31, 2009, our gross margin decreased by 8.0 percentage points when compared to the same period last year. The net gross margin reduction is mainly attributable to our strategy to maintain volume in the market we serve by keeping its pricing competitiveness, and expenses incurred by our new Lab for rent and equipment depreciation in the aggregate amount of approximately \$65,000.

Selling, General and Administrative Expenses. Selling, general and administrative expenses for the three months ended in January 31, 2009 were approximately \$712,000, a reduction of \$104,000 as compared to the same period last year. The net decrease in expenses is mainly attributable to the expense containment measures implemented from last fiscal year and continued in the current fiscal year, geared to offset the service revenue decline and the variance in some expenses incurred by our Lab last year while under the development stage for the aggregate amount of approximately \$24,000.

Interest Expense. We have been recognizing imputed interest expense incurred in connection with the long-term obligations originated pursuant to a plan and agreement of merger dated January 25, 2006 for the acquisition of Pharma-PR. This expense decreases as annual payments are made through fiscal year 2009.

Income Taxes Expense. The decrease on income taxes expense is attributable to the decrease of income before income tax. The statutory income tax rate differs to the effective rate mainly due to the new tax activities in Ireland and our Lab which do not have previous taxable income where their current net operating losses could be carried back and derive a tax benefit. It is company policy to recognize tax benefits of net operating losses when realized. Realization of future tax benefits is dependent on many factors, including the tax activity ability to generate taxable income. Accordingly the income tax benefit will be recognized on a yearly basis when realized.



Net Income. Our net income for the three months ended January 31, 2009 was approximately \$19,000, a decline of \$264,000 or a reduction in profit margin of 7.1 percentage points when compared to the same period last year. For the three months ended in January 31, 2009, earnings per common share basic and diluted were \$0.009, they declined by \$0.005 and \$0.004, respectively, when compared to the same period last year.

Our net income was affected by the decrease in gross margin, partially offset by cost containment measures in selling, general and administrative expenses, favorable variances in interest expense, and the reduction of income tax expense due to the decline in taxable income.

#### Liquidity and Capital Resources

Liquidity is a measure of our ability to meet potential cash requirements, including planned capital expenditures. For the three months ended January 31, 2009, we have generated cash flow from operations of approximately \$0.9 million and working capital of approximately \$2.5 million, notwithstanding within that period we have made a partial payment of \$2.25 million related to the final \$2.75 million installment due in January 2009 pursuant the 2006 Pharma-PR acquisition agreement. If our profitability and liquidity improves, during fiscal year 2009 we expect to pay from working capital the remaining balance of \$500,000.

To the extent that we pursue possible opportunities and are able to expand our operations, either by acquisition or by the establishment of operations in a new locale, we will incur additional overhead, and there may be a delay between the period we commence operations and our generation of net cash flow from operations.

Our primary cash needs consist of the payment of compensation to our professional staff, overhead expenses, statutory taxes, and payments pursuant to the agreement terms for the acquisition of Pharma-PR.

Management believes that with improved levels of operations and cash flows from operations, the collectability of high quality customer receivables will be sufficient to fund anticipated expenses and satisfy other possible long-term contractual commitments, including our obligations to pay the balance of the final installment due in connection with the acquisition of Pharma-PR and our obligations to pay the installment payments due in connection with the acquisition of Integratek, for the next twelve months.

While uncertainties relating to the current local and global economic condition, competition, the industries and geographical regions served by us and other regulatory matters exist within the consulting services industry, management is implementing marketing and cost containment strategies to seek and improve our current liquidity and profitability trend.

#### Off-Balance Sheet Arrangements

We were not involved in any significant off-balance sheet arrangement during the three months ended January 31, 2009.

#### Critical Accounting Policies and Estimates

There were no material changes during the three months ended January 31, 2009 to the critical accounting policies reported in our Annual Report on Form 10-K for the fiscal year ended October 31, 2008.

#### New Accounting Pronouncements

There were no new accounting pronouncements, issued since our filing of the Annual Report on Form 10-K for the fiscal year ended October 31, 2008, which could have a significant effect on our condensed consolidated financial statements.

## Forward-Looking Statements

Our business, financial condition, results of operations, cash flows and prospects, and the prevailing market price and performance of our common stock, may be adversely affected by a number of factors, including the matters discussed below. Certain statements and information set forth in this Quarterly Report on Form 10-Q, as well as other written or oral statements made from time to time by us or by our authorized executive officers on our behalf, constitute “forward-looking statements” within the meaning of the Federal Private Securities Litigation Reform Act of 1995. These statements include all statements other than those made solely with respect to historical fact and identified by words such as “believes”, “anticipates”, “expects”, “intends” and similar expressions, but such words are not the exclusive means of identifying such statements. We intend for our forward-looking statements to be covered by the safe harbor provisions for forward-looking statements contained in the Private Securities Litigation Reform Act of 1995, and we set forth this statement and these risk factors in order to comply with such safe harbor provisions. You should note that our forward-looking statements speak only as of the date of this Quarterly Report on Form 10-Q or when made and we undertake no duty or obligation to update or revise our forward-looking statements, whether as a result of new information, future events or otherwise. Although we believe that the expectations, plans, intentions and projections reflected in our forward-looking statements are reasonable, such statements are subject to known and unknown risks, uncertainties and other factors that may cause our actual results, performance or achievements to be materially different from any future results, performance or achievements expressed or implied by the forward-looking statements. The risks, uncertainties and other factors that our stockholders and prospective investors should consider include, but are not limited to, the following:

- Because our business is concentrated in the pharmaceutical industry in Puerto Rico, any changes in that industry could impair our ability to generate revenue and realize a profit.
- Because our business is dependent upon a small number of clients, the loss of a major client could impair our ability to operate profitably.
- Since our business is dependent upon the development and enhancement of patented pharmaceutical products or processes by our clients, the failure of our clients to obtain and maintain patents could impair our ability to operate profitably.
  - We may be unable to pass on increased labor costs to our clients.
  - Our cash requirements include payments due from our reverse merger transaction.
  - Consolidation in the pharmaceutical industry may have a harmful effect on our business.
- Because the pharmaceutical industry is subject to government regulations, changes in government regulations relating to this industry may affect the need for our services.
- Changes in tax benefits may affect the willingness of companies to continue or expand their operations in Puerto Rico.
- Puerto Rico’s economy, including its governmental financial crisis, may affect the willingness of businesses to commence or expand operations in Puerto Rico.
- Other factors, including economic factors, may affect the decision of businesses to continue or expand their operations in Puerto Rico.
  - If we are unable to protect our clients’ intellectual property, our ability to generate business will be impaired.
- We may be subject to liability if our services or solutions for our clients infringe upon the intellectual property rights of others.
  - We may be held liable for the actions of our employees or contractors when on assignment.
- To the extent that we perform services pursuant to fixed-price or incentive-based contracts, our cost of services may exceed our revenue on the contract.
- Because most of our contracts may be terminated on little or no advance notice, our failure to generate new business could impair our ability to operate profitably.
- Because we are dependent upon our management, our ability to develop our business may be impaired if we are not able to engage skilled personnel.

- We may not be able to continue to grow unless we consummate acquisitions or enter markets outside of Puerto Rico.

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- If we identify a proposed acquisition, we may require substantial cash to fund the cost of the acquisition.
  - If we make any acquisitions, they may disrupt or have a negative impact on our business.
    - Because of our cash requirements, we may be unable to pay dividends.
- Because there is a limited market in our common stock, stockholders may have difficulty in selling our common stock and our common stock may be subject to significant price swings.
- Our quarterly revenues, operating results and profitability will vary from quarter to quarter, which may result in increased volatility of our stock price.
- The issuance of securities, whether in connection with an acquisition or otherwise, may result in significant dilution to our stockholders.

#### ITEM 4. CONTROLS AND PROCEDURES.

##### Evaluation of Disclosure Controls and Procedures

We carried out an evaluation, under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, of the effectiveness of our disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) as of the end of the period covered by this Quarterly Report. Based upon that evaluation, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were effective as of the end of the period covered by this Quarterly Report.

##### Changes in Internal Control Over Financial Reporting

Based on an evaluation, under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, there has been no change in our internal control over financial reporting during our last fiscal quarter identified in connection with that evaluation that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

PART II- OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS.

From time to time, we may be a party to legal proceedings incidental to our business. We do not believe that there are any proceedings threatened or pending against us, which, if determined adversely to us, would have a material effect on our financial position or results of operations and cash flows.

ITEM 6. EXHIBITS

(a) Exhibits:

4.1 Form of First Amendment to Series C Common Stock Purchase Warrant (incorporated by reference to Exhibit 4.1 of the Company's Current Report on Form 8-K filed on January 29, 2009).

10.1 Amendment dated December 17, 2008 to Employment Agreement dated November 5, 2007, between Pedro Lasanta and the Company (incorporated by reference to Exhibit 10.1 of the Company's Current Report on Form 8-K filed on December 23, 2008).

31.1 Certification of chief executive officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

31.2 Certification of chief financial officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

32.1 Certification of the chief executive officer and chief financial officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.



SIGNATURES

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

PHARMA-BIO SERV, INC.

/s/ Elizabeth Plaza  
Elizabeth Plaza  
Chief Executive Officer  
(Principal Executive Officer)

/s/ Pedro J. Lasanta  
Pedro J. Lasanta  
Chief Financial Officer  
(Principal Financial Officer and Principal Accounting Officer)

Dated: March 17, 2009