

Pharma-Bio Serv, Inc.  
Form 10-K  
January 29, 2014

---

---

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

FORM 10-K

(Mark One)

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

For the fiscal year ended October 31, 2013

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,  
#6 Road 696  
Dorado, Puerto Rico  
(Address of Principal Executive Offices)

00646  
(Zip Code)

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

Securities registered pursuant to Section 12(b) of the Act: None

Securities registered pursuant to Section 12(g) of the Act: Common Stock, par value \$0.0001 per share

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.  
Yes  No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes  No

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 for such shorter period that the registrant was

Edgar Filing: Pharma-Bio Serv, Inc. - Form 10-K

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 has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes  No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§229.405 of this chapter) is not contained herein, and will not be contained, to the best of the registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

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 | <input type="checkbox"/> | Accelerated filer         | <input type="checkbox"/> |
| Non-accelerated filer   | <input type="checkbox"/> | Smaller reporting company | <input type="checkbox"/> |

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

The approximate aggregate market value of common stock held by non-affiliates of the registrant, based on the closing price for the registrant's common stock on April 30, 2013 (the last business day of the second quarter of the registrant's current fiscal year), was \$9,054,343.

The number of shares of the registrant's common stock outstanding as of January 28, 2014 was 23,043,094.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the registrant's Proxy Statement relative to the 2014 Annual Meeting of Stockholders are incorporated by reference in Part III hereof.

---

---

PHARMA-BIO SERV, INC.  
FORM 10-K  
FOR THE YEAR ENDED OCTOBER 31, 2013

TABLE OF CONTENTS

|                 |  | Page |
|-----------------|--|------|
| <b>PART I</b>   |  |      |
| ITEM 1          | BUSINESS   | 1    |
| ITEM 1A         | RISK FACTORS   | 7    |
| ITEM 1B         | UNRESOLVED STAFF COMMENTS  | 14   |
| ITEM 2          | PROPERTIES   | 14   |
| ITEM 3          | LEGAL PROCEEDINGS  | 14   |
| ITEM 4          | MINE SAFETY DISCLOSURES  | 14   |
| <b>PART II</b>  |  |      |
| ITEM 5          | MARKET FOR REGISTRANT'S COMMON EQUITY,<br>RELATED STOCKHOLDER MATTERS AND ISSUER<br>PURCHASES OF EQUITY SECURITIES                   | 15   |
| ITEM 6          | SELECTED FINANCIAL DATA  | 16   |
| ITEM 7          | MANAGEMENT'S DISCUSSION AND ANALYSIS OF<br>FINANCIAL CONDITION AND RESULTS OF OPERATIONS<br>QUANTITATIVE AND QUALITATIVE DISCLOSURES | 16   |
| ITEM 7A         | ABOUT MARKET RISK  | 23   |
| ITEM 8          | FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA<br>(See F-1)   | 23   |
| ITEM 9          | CHANGES IN AND DISAGREEMENTS WITH<br>ACCOUNTANTS ON ACCOUNTING AND FINANCIAL<br>DISCLOSURE   | 23   |
| ITEM 9A         | CONTROLS AND PROCEDURES  | 23   |
| ITEM 9B         | OTHER INFORMATION  | 24   |
| <b>PART III</b> |  |      |
| ITEM 10         | DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE<br>GOVERNANCE  | 25   |
| ITEM 11         | EXECUTIVE COMPENSATION   | 25   |
| ITEM 12         | SECURITY OWNERSHIP OF CERTAIN BENEFICIAL<br>OWNERS AND MANAGEMENT AND RELATED<br>STOCKHOLDER MATTERS                                 | 25   |
| ITEM 13         | CERTAIN RELATIONSHIPS AND RELATED<br>TRANSACTIONS, AND DIRECTOR INDEPENDENCE   | 25   |
| ITEM 14         | PRINCIPAL ACCOUNTING FEES AND SERVICES   | 25   |
| <b>PART IV</b>  |  |      |
| ITEM 15         | EXHIBITS, FINANCIAL STATEMENT SCHEDULES  | 26   |

SIGNATURES

29

FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

F-1

## PART I

### ITEM 1. BUSINESS.

#### GENERAL

Pharma-Bio Serv, Inc. is a Delaware corporation, organized in 2004 under the name Lawrence Consulting Group, Inc. In February 2006, our corporate name was changed to Pharma-Bio Serv, Inc.

On January 25, 2006, pursuant to an agreement and plan of merger among us, Plaza Acquisition Corp., Pharma-Bio Serv PR, Inc. (then known as Plaza Consulting Group, Inc. and referred to as “Pharma-PR”), and the then sole stockholder of Pharma-PR, Plaza Acquisition Corp. was merged into Pharma-PR, with the result that Pharma-PR became our wholly-owned subsidiary and our sole business became the business of Pharma-PR.

Pharma-PR business was established as a sole proprietorship in 1993 and incorporated in 1997 to offer compliance consulting services to the pharmaceutical industry. The business operations provide services to the pharmaceutical, biotechnology, medical device and chemical manufacturing companies principally in Puerto Rico, the United States and Europe.

Our executive offices are located at Pharma-Bio Serv Building, #6 Road 696, Dorado, Puerto Rico 00646. Our telephone number is (787) 278-2709. The financial information about our reporting segments appear in Note K to our Consolidated Financial Statements included in this Annual Report on Form 10-K.

Our website is [www.pharmabioserv.com](http://www.pharmabioserv.com). Information on our website or any other website is not part of this Annual Report on Form 10-K.

References to “we,” “us,” “our” and similar words in this Annual Report on Form 10-K refer to Pharma-Bio Serv, Inc. and its subsidiaries.

#### OVERVIEW

We are a compliance, project management and technology transfer support consulting firm with a laboratory testing facility 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, dedicated validation and compliance consulting firms, large publicly traded and private domestic and foreign engineering and consulting firms. We provide a broad range of compliance related consulting services. We also provide microbiological testing services and chemical testing services through our laboratory testing facility (“Lab”) in Puerto Rico. In addition, we provide information technology consulting services and technical training/seminars, which services are not currently significant to our operating results. We market our services to pharmaceutical, chemical, biotechnology and medical devices, and allied products companies in Puerto Rico, the United States and Europe. Our team includes more than 300 experienced engineering and life science professionals, and includes former quality assurance managers and directors, and experienced and trained professionals with bachelors, masters and doctorate degrees in health sciences and engineering.

We have a well-established and consistent relationship with the major pharmaceutical, biotechnology, medical device and chemical manufacturing companies in Puerto Rico and the United States, which provides us access to affiliated companies in other markets. We seek opportunities in markets that can yield profitable margins using our professional consulting force and also provide services such as those performed by our microbiological testing laboratory facility, our information technology service division, Integratek, and our technical training division, Pharma Serv Academy.

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. Our Pharma Serv Academy division, through a network of leading industry professional experts in their field, which include resources of our own, provides technical seminars/training that incorporates the latest regulatory trends and standards as well as other related areas. Although these services are not currently significant to our operating results, 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.

We believe the most significant factors to achieving future business growth includes: (i) industry participants' need for compliance consulting and contingent resources support services; (ii) our ability to recruit and retain highly educated and experienced professionals to meet those customer's needs; (iii) our ability to further expand our offerings and services to address the changing needs of our clients; and (iv) our ability to expand our market presence in the United States, Europe and possibly other emerging pharmaceutical markets in order to respond to the international compliance needs of our clients. Our business is affected to the extent the current economic downturn and changing regulations affect the decision of our clients and potential clients to establish operations or to continue or expand their existing operations.

Our revenue is derived from (i) time and materials contracts (representing approximately 92% of total revenue), where the clients are charged for the time, materials and expenses incurred on a particular project or service, (ii) fixed-fee contracts or from "not to exceed" contracts (approximately 2% of total revenue), which are generally short-term contracts, in which the value of the contract cannot exceed a stated amount, and (iii) laboratory testing (representing approximately 6% of total revenue) which generally is completed and certified within days of sample receipt. For time and materials contracts, our revenue is principally a function of the number of resources and the number of hours billed per professional. To the extent that our revenue is based on fixed-fee or "not to exceed" contracts, our ability to operate profitably is dependent upon our ability to estimate accurately the costs that we will incur on a project and to manage and monitor the project. If we underestimate our costs on any contract, we could sustain a loss on the contract or its profitability might be reduced.

The principal components of our costs of services are resource compensation (salaries and wages, independent contractors' fees, taxes and benefits) and expenses relating to the performance of the services. In order to ensure that our pricing is competitive yet minimize the impact on our margins, we manage increasing labor costs by (i) selecting resources according to our cost for specific projects, (ii) negotiating, where applicable, compensation packages with the resource, (iii) subcontracting labor and (iv) negotiating and passing rate increases to our customers, as applicable. Although this strategy has been successful in the past, we cannot give any assurance that such strategy will continue to be successful. As for our laboratory testing operation, the major costs of services components are salaries and wages, occupancy and depreciation expenses, plus consumable goods usage.

We have established quality systems for our employees which include:

Training Programs - including a current Good Manufacturing Practices exam prior to recruitment and periodic refreshers;

Recruitment Full Training Program - including employee manual, dress code, time sheets and good project management and control procedures, job descriptions, and firm operating and administration procedures;

Safety Program - including OSHA, Environmental Health and Safety; and

Code of Ethics and Business Conduct - a code of ethics and business conduct is used and enforced as one of the most significant company controls on personal behavior.

In addition, we have implemented procedures to respond to client complaints and have in place customer satisfaction survey procedures. As part of our employee performance review, our clients receive an evaluation form for employee project performance feedback, including compliance with our code of ethics and business conduct.

## BUSINESS STRATEGY AND OBJECTIVES

We are actively pursuing new markets as part of our growth strategy. We have a well-established and consistent relationship with the major pharmaceutical, biotechnology, medical device and chemical manufacturing companies in Puerto Rico and the United States which provides us access to affiliated companies in other markets. We seek opportunities in markets that can yield profitable margins using our professional consulting force and also provide new services such as those performed by our microbiological testing laboratory facility.

Our business strategy is based on a commitment to provide premium quality and professional consulting services and reliable customer service to our customer base. Our business strategy and objectives are as follow:

Continue growth in consulting services in each technical service, quality assurance, regulatory compliance, technology transfer, validation, project management, laboratory testing, technical training and greater market penetration from our marketing and sales efforts;

Continue to enhance our technical consulting services through internal growth and acquisitions that provide solutions to our customers' needs;

Motivate our professionals and support staff by implementing a compensation program which includes both individual performance and overall company performance as elements of compensation;

Create a pleasant corporate culture and emphasize operational quality safety and timely service;

Continue to maintain our reputation as a trustworthy and highly ethical partner; and

Efficiently manage our operating and financial costs and expenses.

### 2006 U.S. Validation Compliance Service Business Acquisition

In January 2006, we acquired a validation compliance service business which served as the foundation to enter the United States market. As of October 31, 2013, the United States market represents approximately 34% of the Company's revenues.

### 2007 Entrance to Ireland Market

In September 2007, through the formation of an Irish subsidiary, we entered into the Ireland market with the intent to provide the same consulting services in Ireland as we provide in the Puerto Rico and United States markets.

### 2008 Integratek Acquisition

In December 2008, we acquired through one of our subsidiaries the operations and assets of Integratek Corp. ("Integratek"), an information technology services and consulting firm based in Puerto Rico. With this acquisition, we broaden the portfolio of services to our customer base and also target other potential customers in other industries.



#### 2009 Laboratory Testing Facility

Our laboratory testing facility ("Lab") located in Puerto Rico, with an investment of \$1.5 million for microbiology, chemical and environmental testing, commenced operations in early fiscal 2009. The Lab is U.S. Food and Drug Administration ("FDA") registered and ISO 9001 certified. The Lab was also recently certified by the European Medicines Agency ("EMA"). The Lab incorporates the latest technology and test methodologies meeting pharmacopoeia industry standards and regulations. It offers testing and related services to our core industries already serviced as well as the cosmetic and food industries.

#### 2012 Entrance to Spain Market

In January 2012, we initiated a consulting services operation to the Spanish market. Currently, these services are covered under a Spanish subsidiary. Consulting services provided in the Spanish market are similar to those covered in the other markets we serve.

#### 2013 Minority Controlled Company Certification

In line with the strategy to penetrate the United States market, on September 24, 2013, we obtained the renewal of the certification as a "minority-controlled company" as defined by the National Minority Supplier Development Council and Growth Initiative ("NMSDC"). The certification allows us to participate in corporate diversity programs available from various potential customers in the United States and Puerto Rico. The Company has maintained this certification since July 2008. The certification is subject to renewal on September 24, 2014. Among others, (i) at least 30% minority ownership and (ii) minority company control are part of the requirements for re-certification.

#### TECHNICAL CONSULTING SERVICES

We have established a reputation as a premier technical consulting services firm to the pharmaceutical, biotechnology, medical device and chemical manufacturing industries in various markets. These services include regulatory compliance, validation, technology transfer, engineering, project management and process support. We have approximately 25 clients that are among the largest pharmaceutical, chemical manufacturing, medical device and biotechnology companies. We are actively participating in exhibitions, conferences, conventions and seminars as either exhibitors, sponsors or conference speakers.

#### MARKETING

We conduct our marketing activities in Puerto Rico, United States, Europe and other marketplaces. We actively utilize our project managers and leaders who are currently managing consulting service contracts at various client locations to also market consulting and laboratory testing services to their existing and past client relationships. 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.

#### PRINCIPAL CUSTOMERS

We provide a substantial portion of our services to three customers, each of whom accounted for 10% or more of our revenues in the years ended October 31, 2013 and 2012. During the years ended October 31, 2013 and 2012, these customers accounted for, in the aggregate, 55% and 52% of total revenue, respectively. In spite of the fact that just a few customers represent a significant source of revenue, our functions are not a continuous process. Accordingly, the

client base for which our services are typically rendered, on a project-by-project basis, changes regularly. Therefore, in any given year a small number of customers could represent a significant source of our revenue for that year. The loss of, or significant reduction in the scope of work performed for any major customer or our inability to replace customers upon completion of contracts could adversely affect our revenue and impair our ability to operate profitably.

## COMPETITION

We are engaged in a highly competitive and fragmented industry. Some of our competitors are, on an overall basis, larger than we are or are subsidiaries of larger companies, and therefore may possess greater resources than we do. Furthermore, because the technical professional aspects of our consulting business do not usually require large amounts of capital, there is relative ease of market entry for a new entrant possessing acceptable professional qualifications. Accordingly, we compete with regional, national, and international firms, large and small. Within the Puerto Rico, United States and Europe markets, certain competitors, including local competitors, may possess greater resources than we do as well as better access to clients and potential clients.

Competition for validation and consulting services used to be primarily based on reputation, track record, experience, and quality of service. However, given the economic recession and our clients' strategies to reduce costs, price of service has become a major factor in sourcing our services. We believe we enjoy competitive advantages over other consulting service firms because of our historical market share within Puerto Rico (20 years), brand name, reputation and track record with many of the major pharmaceutical, biotechnology, medical device and chemical manufacturing companies, which have a presence in the markets we are pursuing.

The market of qualified and experienced professionals that are capable of providing technical consulting services is very competitive and consists primarily of our competitors as well as companies in the pharmaceutical, chemical, biotechnology and medical device industries who are our clients and potential clients. In seeking qualified personnel, we market our name recognition in the Puerto Rico market, our reputation with our clients and salary and benefit packages.

## RAW MATERIALS

We require the use of various raw materials, including culture media, DNA reagents, LAL reagents and biological indicators, in our testing laboratory facility. We purchase these raw materials from various suppliers. At times, we concentrate orders among a few suppliers in order to strengthen our supplier relationships and receive quantity discounts. Raw materials are generally available from multiple suppliers at competitive prices, and amounts kept in stock are not significant.

## ENVIRONMENTAL REGULATIONS

Activities in our laboratory testing facility are regulated under Puerto Rico and U.S. federal laws designed to protect workers and the environment. Some of these laws include the Occupational Safety and Health Act and the Resource Conservation and Recovery Act. These laws apply to the use, handling and disposal of various biological and chemical substances used in our processes. We believe we are in material compliance with these laws and that continued compliance will not have a materially adverse effect on our business. No specific accounting for environmental compliance has been maintained or projected by us at this time.

## INTELLECTUAL PROPERTY RIGHTS

We have no proprietary software or products. We rely on non-disclosure agreements with our employees to protect the proprietary software and other proprietary information of our clients. Any unauthorized use or disclosure of this information could harm our business.

## EMPLOYEES

We employ approximately 220 employees, all of whom are full time employees. None of our employees are represented by a labor union, and we consider our employee relations to be good.

## EXECUTIVE OFFICERS

The following table sets forth certain information with respect to our executive officers.

| Name             | Age | Position  |
|------------------|-----|---|
| Elizabeth Plaza  | 50  | Chairman and Principal Executive Officer                                |
| Nélida Plaza     | 46  | Chief Operating Officer and Secretary                                   |
| Pedro J. Lasanta | 54  | Chief Financial Officer and Vice President - Finance and Administration |

Elizabeth Plaza has served as the Chairman of the Board since January 2006 and our Principal Executive Officer since January 1, 2014. Also, Ms. E. Plaza assumed the role of Senior Strategic Consultant of the Company on January 1, 2013. Ms. E. Plaza served as our president and chief executive officer from January 2006 to December 2012. Ms. E. Plaza holds a B.S. in Pharmaceutical Sciences, magna cum laude, from the School of Pharmacy of the University of Puerto Rico. She was a 40 under 40 Caribbean Business Award recipient in 2002, the 2003 recipient of Ernst & Young's Entrepreneur of the Year Award in Health Science, one of the 2003 recipients of the Puerto Rico Powerful Business Women Award, elected as Puerto Rico Manufacturers Association 2004 (Metropolitan-West Region) Executive of the Year, and Puerto Rico 2008 Executive of the Year. She is member of the US Department of Commerce National Advisory Council on Minority Business Enterprise and is also member of the Puerto Rico Manufacturer's Association Board of Directors.

Nélida Plaza has served as our Chief Operating Officer since January 1, 2014 and our Secretary since January 2006. Ms. N. Plaza previously served as the Company's Acting President and Chief Executive Officer from January 2013 until December 31, 2013, Vice President of Operations of Pharma-Bio Serv PR, Inc. from January 2004 until December 31, 2013, and the Company's President of Puerto Rico Operations from December 2009 until December 31, 2013. In July 2000, Ms. N. Plaza joined Pharma-PR as a project management consultant. In the past, Ms. N. Plaza was a Unit Operations Leader and Safety Manager at E.I. DuPont De Nemours where she was in charge of all manufacturing operations and was involved with the development, support and audit of environmental, safety and occupational health programs. Ms. N. Plaza holds a M.S. in Environmental Management from the University of Houston in Clear Lake and a B.S. in Chemical Engineering from the University of Puerto Rico. Ms. N. was recognized by Casiano Communications as one of the 40 under 40 distinguished executives in Puerto Rico. Ms. N. and Elizabeth Plaza are sisters.

Pedro J. Lasanta has served as our Chief Financial Officer and Vice President - Finance and Administration since November 2007. From 2006 until October 2007, Mr. Lasanta was in private practice as an accountant, tax and business counselor. From 1999 until 2006, Mr. Lasanta was the Chief Financial Officer for Pearle Vision Center PR, Inc. In the past, Mr. Lasanta was also an audit manager for Ernst & Young, formerly Arthur Young & Company. He is a cum laude graduate in business administration (accounting) from the University of Puerto Rico. Mr. Lasanta is a Certified Public Accountant. In 2012, he was awarded the Puerto Rico Manufacturers Association (North Region) Service Manager of the Year.

## ITEM 1A. RISK FACTORS.

This Annual Report on Form 10-K includes “forward-looking statements” within the meaning of Section 21E of the Securities Exchange Act of 1934, as amended, including, in particular, certain statements about our plans, strategies and prospects. Although we believe that our plans, intentions and expectations reflected in or suggested by such forward-looking statements are reasonable, we cannot assure you that such plans, intentions or expectations will be achieved. Important factors that could cause our actual results to differ materially from our forward-looking statements include those set forth in this Risk Factors section.

If any of the following risks, or other risks not presently known to us or that we currently believe to not be significant, develop into actual events, then our business, financial condition, results of operations, cash flows or prospects could be materially adversely affected.

### Risks That Relate to our Business

Because our business is concentrated in the pharmaceutical industry in Puerto Rico, the United States and Europe, any changes in that industry or in those markets could impair our ability to generate revenue and realize a profit.

Since most of our business is performed in Puerto Rico, the United States and Europe, for pharmaceutical, biotechnology, medical device and chemical manufacturing companies, our ability to generate revenue and realize a profit could be impaired by factors impacting those markets. For example, changes in tax laws or regulatory, political or economic conditions, which discourage businesses from operating in the markets we serve, which affect the need for services such as those provided by us, could impair our ability to generate revenue and realize a profit.

The pharmaceutical industry in Puerto Rico has been decreasing and we believe it will continue to decrease mostly due to the excess capacity the industry is facing due to a reduction in new product launches and expiring patents, thus impacting capital investment, which typically would bring in validation business. Also, the migration of labor intensive manufacturing businesses to markets with generally lower labor costs, such as Asia and South America, will continue to further reduce the presence of labor of chemical and pharmaceutical companies in Puerto Rico.

Puerto Rico government enacted ACT 154 of October 22, 2010 which may adversely affect the willingness of our customers to do business in Puerto Rico and consequently adversely affect our business.

On October 22, 2010, Act No. 154 was enacted by the Puerto Rico government. The act primarily affects the industry we serve and consequently our customer base. Act 154 extends the circumstances under which a nonresident alien individual or a non resident corporation or partnership can be treated as doing business in Puerto Rico and is deriving income from sources within Puerto Rico for purposes of income tax. It also provides for the imposition of a temporary excise tax on some acquisitions by non-resident individuals, corporations or partnerships, of products totally or partially manufactured or produced in Puerto Rico and of related services to said products of affiliated entities with the buyer. It basically adopts a modified income sourcing rule and a temporary excise tax that will be enforced for a period of six (6) years and will decrease gradually during this time.

The impact of the act, if any, over the industry and its willingness to do business in Puerto Rico continues to be uncertain. Consequently, our ability to generate revenue in Puerto Rico may be impaired.

Changes in tax benefits may affect the willingness of companies to continue or expand their operations in Puerto Rico.

Until 1996, the Internal Revenue Code provided certain tax benefits to pharmaceutical companies operating in Puerto Rico by enabling their Puerto Rico operations to operate free from federal income taxes. Partly as a result of the tax

benefits, numerous pharmaceutical companies established facilities in Puerto Rico. In 1996, this tax benefit was eliminated, although companies that had facilities in Puerto Rico could continue to receive these benefits for ten years, at which time the benefits were set to expire. In order to promote business activities in Puerto Rico, in May 2008 the Puerto Rico government enacted a tax incentive law (“Act 73”). Act 73 provides tax exemption from various taxes, including income tax, and investment credits for activities similar to those of our customers and our company. The change in the tax laws may affect favorably or unfavorably the willingness of pharmaceutical companies to continue or to expand their Puerto Rico operations. To the extent that pharmaceutical companies choose to develop and manufacture products outside of Puerto Rico, our ability to generate new business may be adversely impaired.

Puerto Rico’s economy, including its governmental financial crisis, may affect the willingness of other businesses to commence or expand operations in Puerto Rico.

As a result of Puerto Rico’s governmental financial crisis, other businesses may be reluctant to establish or expand their operations in Puerto Rico, and in some case, these businesses may consider closing existing operations carried in Puerto Rico. Further, since Puerto Rico’s economy is petroleum-based, the fluctuating price of oil, combined with Puerto Rico’s high level of debt, may make Puerto Rico a less attractive place to expand existing operations or commence new business activities. To the extent that companies in the pharmaceutical and related industries decide not to commence new operations or expand their existing operations in Puerto Rico, or if these businesses close existing operations in Puerto Rico, the market for our services may decline.

Other factors, including economic factors, may affect the decision of businesses to continue or expand their operations in the markets we serve.

Companies in the pharmaceutical and related industries for which we perform service are subject to economic pressures, which affect their global operations and which may influence the decision to reduce or increase the scope of their operations in the markets we serve. These companies consider a wide range of factors in making such a decision, and may be influenced by a need to consolidate operations, to reduce expenses, to increase their business in geographical regions where there are large customer bases, tax, regulatory and political considerations and many other factors. We cannot assure you that our customers and potential customers will not make extensive reductions or terminate their operations in the markets we serve entirely, which could significantly impair our ability to generate revenue.

Our business and operating results may be adversely impacted if we are unable to maintain our certification as a minority-controlled company.

On September 24, 2013, we obtained the renewal of the certification as a "minority-controlled company" as defined by the National Minority Supplier Development Council and Growth Initiative ("NMSDC"). The certification allows 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 September 24, 2014. Among others, (i) at least 30% minority ownership and (ii) minority company control are part of the requirements for re-certification. Our business and operating results may be adversely impacted if we are unable to maintain our certification as a minority-controlled company.

Because our business is dependent upon a small number of clients, the loss of a major client could impair our ability to operate profitably.

Our business has been dependent upon a small number of clients. During the years ended October 31, 2013 and 2012, a small number of clients accounted for a disproportionately large percentage of our revenue. In the years ended October 31, 2013 and 2012, three customers accounted for, in aggregate, approximately 55% and 52% of total revenue, respectively.

The loss of, or significant reduction in the scope of work performed for, or any significant change in the financial terms related to, any major customer, could impair our ability to operate profitably. We cannot assure that we will not sustain significant decreases in revenue from our major customers or that we will be able to replace any major customers or the resulting decline in revenue.

Customer procurement and sourcing practices intended to reduce costs could have an adverse affect on our margins and profitability.

In an effort to reduce their costs, many of our customers are establishing or extending the scope of their procurement departments to include consulting and project management services, such as ours. As a result, we have less interaction with the end user of our services (typically Quality Control or Manufacturing Operations Leaders) when bidding on a project, which we believe decreases the focus on the quality of service provided and increases the emphasis on cost of the service. This may cause us to lower the price of our bids, which would reduce the margins in a given project. Also, some customers have established vendor management/vendor neutral-programs with third-parties (some of whom are also our competitors). Because these vendor management programs may receive a percentage of our fees, without a corresponding increase in the fee itself, our margins would decline. In addition, where a vendor management program is a competitor for a particular service we provide, we may have difficulty securing that particular business, which would adversely impact volume and revenue. Some of these vendor neutral programs intend to limit our interaction



with our direct end user, and our interaction is limited to the representative of the vendor neutral agency. This limitation impairs our ability to establish and maintain our relationships with our customers and recognition of the value added in the service.

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.

Companies in the pharmaceutical industry are highly dependent on their ability to obtain and maintain patents for their products or processes. The inability to obtain new patents and the expiration of active patents may reduce the need for our services and thereby impair our ability to operate profitably.

We may be unable to pass on increased labor costs to our clients.

The principal components of our cost of revenues are employee compensation (salaries, wages, taxes and benefits) and expenses relating to the performance of the services we provide. We face increasing labor costs which we seek to pass on to our customers through increases in our rates. To remain competitive, we may not be able to pass these increased costs on to our clients, and, to the extent that we are not able to pass these increased costs on to our clients, our gross margin will be reduced.

Consolidation in the pharmaceutical industry may have a harmful effect on our business.

In recent years, the pharmaceutical industry has undergone consolidation, and may in the future undergo further substantial consolidation which may reduce the number of our existing and potential customers. The consolidation in the pharmaceutical industry may have a harmful effect on our business and or ability to maintain and replace customers.

Because the pharmaceutical industry is subject to government regulations, changes in government regulations relating to this industry may affect the need for our services.

Because government regulations affect all aspects of the pharmaceutical, biotechnology, medical device and chemical manufacturing industries, including regulations relating to the testing and manufacturing of pharmaceutical products and the disposal of materials which are or may be considered toxic, any change in government regulations could have a profound effect upon not only these companies but companies, such as ours, that provide services to these industries. If we are not able to adapt and provide necessary services to meet the requirements of these companies in response to changes in government regulations, our ability to generate business may be impaired.

Our reputation and divisions may be impacted by regulatory standards impacting our customer products.

We provide microbiological and chemical testing services to our customer products that are distributed worldwide. Any concerns regarding our customer products complying with regulatory standards could result in inquiries regarding our laboratory or testing services. As a result, we may need to participate in litigation or regulatory audits requiring the investment of significant time and funds. In addition, the reputation of our Lab and technical services, as well as our technical expertise, might suffer. Furthermore, any such inquiries or any adverse impact of such inquiries may financially impact our Lab and other divisions, including our consulting division.

If we are unable to protect our clients' intellectual property, our ability to generate business will be impaired.

Our services either require us to develop intellectual property for clients or provide our personnel with access to our clients' intellectual property. Because of the highly competitive nature of the pharmaceutical, biotechnology, medical device and chemical manufacturing industries and the sensitivity of our clients' intellectual property rights, our ability to generate business would be impaired if we fail to protect those rights. Although all of our employees and contractors are required to sign non-disclosure agreements, any disclosure of a client's intellectual property by an employee or contractor may subject us to litigation and may impair our ability to generate business either from the affected client or other potential clients. In addition, we are required to enter into confidentiality agreements and our failure to protect the confidential information of our clients may impair our business relationship.

We may be subject to liability if our services or solutions for our clients infringe upon the intellectual property rights of others.

It is possible that in performing services for our clients, we may inadvertently infringe upon the intellectual property rights of others. In such event, the owner of the intellectual property may commence litigation seeking damages and an injunction against both us and our client, and the client may bring a claim against us. Any infringement litigation would be costly, regardless of whether we ultimately prevail. Even if we prevail, we will incur significant expenses and our reputation would be hurt, which would affect our ability to generate business and the terms on which we would be engaged, if at all.

We may be held liable for the actions of our employees or contractors when on assignment.

We may be exposed to liability for actions taken by our employees or contractors while on assignment, such as damages caused by their errors, misuse of client proprietary information or theft of client property. Due to the nature of our assignments, we cannot assure you that we will not be exposed to liability as a result of our employees or contractors being 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.

Some of our revenue is derived from fixed-price contracts. Our costs of services may exceed revenue of these contracts if we do not accurately estimate the time and complexity of an engagement. Further, we are seeking contracts by which our compensation is based on specified performance objectives, such as the realization of cost savings, quality improvements or other performance objectives. Our failure to achieve these objectives would reduce our revenue and could impair our ability to operate profitably.

Our profit margin is largely a function of the rates we are able to charge and collect for our services and the utilization rate of our professionals. Accordingly, if we are not able to maintain our pricing for our services or an appropriate utilization rate for our professionals without corresponding cost reductions, our profit margin and profitability will suffer. The rates we are able to charge for our services are affected by a number of factors, including:

Our clients' perception of our ability to add value through our services;

Our ability to complete projects on time;

Pricing policies of competitors;

Our ability to accurately estimate, attain and sustain engagement revenues, margins and cash flows over increasingly longer contract periods; and

General economic and political conditions.

Our utilization rates are also affected by a number of factors, including:

Our ability to move employees and contractors from completed projects to new engagements; and

Our ability to manage attrition of our employees and contractors.

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.

Most of our contracts can be terminated by our clients with little or no advance notice. Our clients typically retain us on a non-exclusive, engagement-by-engagement basis, and the client may terminate, cancel or delay any engagement or the project for which we are engaged, at any time and on no advance notice. As a result, the termination, cancellation, expiration or delay of contracts could have a significant impact on our ability to operate profitably.

Because of the competitive nature of the pharmaceutical, biotechnology, medical device and chemical manufacturing consulting market, we may not be able to compete effectively if we cannot efficiently respond to changes in the structure of the market and developments in technology. For example, changes in the consulting business model to a

pure staffing and contingent workforce driven primarily by pricing pressure represents a major threat to our competitive advantage.

Because of recent consolidations in the pharmaceutical, biotechnology, medical device and chemical manufacturing consulting business, we are faced with an increasing number of larger companies that offer a wider range of services and have better access to capital than we have. We believe that larger and better-capitalized competitors have enhanced abilities to compete for both clients and skilled professionals. Also, smaller private local firms may have a greater capacity to respond faster to customers' requests and to better adapt to market changes, such as reduced margins. In addition, one or more of our competitors may develop and implement methodologies that result in superior productivity and price reductions without adversely affecting their profit margins. We cannot assure you that we will be able to compete effectively in an increasingly competitive market.

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.

Our success in the past has depended in large part on the skills and efforts of Elizabeth Plaza, our former President, Chief Executive Officer and founder. Since January 1, 2013, Elizabeth Plaza assumed the role of Senior Strategic Consultant to the Company. Elizabeth's Plaza consulting agreement was renewed effective January 1, 2014 for a term of one year. Nélica Plaza was appointed by the Board to the position of Chief Operating Officer for the Company. Ms. N. Plaza previously served as the Company's Acting President and Chief Executive Officer. It is uncertain if these changes will have a material adverse effect on the development and success of our business.

Our future success will depend in part upon our ability to attract and retain additional qualified management and technical personnel. Our divisional management heads are highly qualified and recognized professionals that may be attracted by pharmaceutical companies or other competitors. Competition for such personnel is intense and we compete for qualified personnel with numerous other employers, including consulting firms, some of which have greater resources than we have, as well as pharmaceutical companies, most of which have significantly greater financial and other resources than we do. We may experience increased costs in order to retain and attract skilled employees. Our failure to attract additional personnel or to retain the services of key personnel and independent contractors could have a material adverse effect on our ability to operate profitably. In addition, although we have contracts with Elizabeth Plaza, Nélica Plaza and our divisional management heads, these agreements do not guarantee that they will continue to work for the Company.

We may not be able to continue to grow unless we consummate acquisitions or enter markets outside of Puerto Rico, the United States, Ireland and Spain.

An important part of our growth strategy is (i) to acquire other businesses which can increase the range of services and products that we can offer and (ii) to establish offices in places where we do not presently operate, either by acquisition or by internal growth. If we fail to make any acquisitions or otherwise expand our business, our future growth may be limited. The success in any market will be dependent on such factors as regulatory, tax, political or economic conditions, our abilities to penetrate the market, hire qualified personnel in a timely manner, obtain and maintain reasonable labor costs, generate service revenue volume and profitable margins.

Any acquisitions we make may be made with cash or our securities or a combination of cash and securities. To the extent that we require cash, we may have to borrow the funds or sell equity securities. We have no commitments from any financing source and we may not be able to raise any cash necessary to complete an acquisition. If we seek to expand our business internally, we will incur significant start-up expenses without any assurance of our ability to penetrate the market.

Our cash could be adversely affected if the financial institutions in which we hold our cash fail.

The Company maintains domestic cash deposits in Federal Deposit Insurance Corporation ("FDIC") insured banks and in money market obligation trusts registered under the US Investment Company Act of 1940, as amended. The domestic bank deposit balances may exceed the FDIC insurance limits. In the foreign markets we serve, we also maintain cash deposits in foreign banks, some of which are not insured or partially insured by the FDIC or other similar agency. These balances could be impacted if one or more of the financial institutions in which we deposit monies fails or is subject to other adverse conditions in the financial or credit markets. To date, we have experienced no loss or lack of access to our invested cash; however, we can provide no assurance that access to our invested cash will not be impacted by adverse conditions in the financial and credit markets.

If we identify a proposed acquisition, we may require substantial cash to fund the cost of the acquisition.

We may require substantial capital or available debt or equity financing to execute on acquisition and expansion opportunities that may come available. We cannot assure you that we will be able to obtain financial resources on terms acceptable to us, or at all. Failure to obtain such financial resources could adversely affect our plans for growth. Until a reliable market providing for sufficient liquidity of our common stock develops, sellers of acquisition candidates may be unwilling to accept our common stock as consideration in a transaction, which could adversely impact our ability to execute on acquisition opportunities.

If we make any acquisitions, they may disrupt or have a negative impact on our business.

If we make acquisitions or establish operations in locales outside of Puerto Rico, we could have difficulty integrating the acquired companies' personnel and operations with our own. In addition, the key personnel of the acquired business may not be willing to work for us. We cannot predict the effect an expansion may have on our core business. Regardless of whether we are successful in making an acquisition, the negotiations could disrupt our ongoing business, distract our management and employees and increase our expenses. In addition to the risks described above, acquisitions are accompanied by a number of inherent risks, including, without limitation, the following:

the difficulty of integrating acquired products, services or operations;

the potential disruption of the ongoing businesses and distraction of our management and the management of acquired companies;

the potential loss of contracts from clients of acquired companies;

the difficulty of maintaining profitability due to increased labor and expenses from acquired companies;

difficulties in complying with regulations in other countries that relate to both the pharmaceutical or other industries to which we provide services as well as our own operations;

difficulties in maintaining uniform standards, controls, procedures and policies;

the potential impairment of relationships with employees and customers as a result of any integration of new management personnel;

the potential inability or failure to achieve additional sales and enhance our customer base through cross-marketing of the products to new and existing customers;

the effect of any government regulations which relate to the business acquired;

potential unknown liabilities associated with acquired businesses or product lines, or the need to spend significant amounts to retool, reposition or modify the marketing and sales of acquired products or the defense of any litigation, whether of not successful, resulting from actions of the acquired company prior to our acquisition;

difficulties in disposing of the excess or idle facilities of an acquired company or business and expenses in maintaining such facilities; and

potential expenses under the labor, environmental and other laws of other countries.

Our business could be severely impaired if and to the extent that we are unable to succeed in addressing any of these risks or other problems encountered in connection with an acquisition. Further, the commencement of business in locales where we have no current operations may be subject to additional significant risks.



## Risks Concerning our Securities

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.

There is a very limited market for our common stock. Since trading commenced in December 2006, there has been little activity in our common stock and on some days there is no trading in our common stock. Because of the limited market for our common stock, the purchase or sale of a relatively small number of shares may have an exaggerated effect on the market price for our common stock. We cannot assure stockholders that they will be able to sell common stock or, that if they are able to sell their shares, that they will be able to sell the shares in any significant quantity at the quoted price.

Our revenues, operating results and profitability will vary from quarter to quarter, which may result in increased volatility of our stock price.

Our quarterly revenues, operating results and profitability have varied in the past and are likely to vary significantly from quarter to quarter, making them difficult to predict. This may lead to volatility in our share price. The factors that are likely to cause these variations are:

Seasonality, including number of workdays and holiday and summer vacations;

The business decisions of clients regarding the use of our services;

Periodic differences between clients' estimated and actual levels of business activity associated with ongoing engagements, including the delay, reduction in scope and cancellation of projects;

The stage of completion of existing projects and their termination;

Our ability to move employees quickly from completed projects to new engagements and our ability to replace completed contracts with new contracts with the same clients or other clients;

The introduction of new services by us or our competitors;

Changes in pricing policies by us or our competitors;

Our ability to manage costs, including personnel compensation, support-services and severance costs;

Acquisition and integration costs related to possible acquisitions of other businesses;

Changes in estimates, accruals and payments of variable compensation to our employees or contractors; and

Global economic and political conditions and related risks, including acts of terrorism.

ITEM 1B. UNRESOLVED STAFF COMMENTS.

Not applicable.

ITEM 2. PROPERTIES.

In February 2012, the Company automatically renewed a lease agreement for our main resource facilities in Dorado, Puerto Rico with an affiliate of Elizabeth Plaza, our Chairman of the Board. These facilities accommodate our testing laboratory, our customer-specialized training facilities, and our Puerto Rico consulting and headquarters offices. The renewal is for a term of five years with monthly rental payments of \$23,930, \$25,127, \$26,383, \$27,702 and \$29,087 for each of the five years then remaining under the lease. The 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.

In November 2011, the Company entered into a lease agreement for the U.S. office facilities located in Plymouth, Pennsylvania. The lease was for a five-year term with monthly rental payments of \$6,282 for the first three years and subsequent increases of four percent per year. During the 2013 fiscal year, the landlord filed for bankruptcy. The lease was renegotiated with a new landlord with an effective date of December 1, 2013. The new lease is for a term of seven years, with monthly rental payments of \$6,282 for the first three years, and \$6,596, \$6,794, \$6,998, and \$7,208, respectively, thereafter. The lease has a renewal option for a term of three years with monthly rental payments of \$7,424, \$7,647 and \$7,876, for each of the years, respectively.

The Company maintains office facilities in Cork, Ireland and Madrid, Spain. Both facilities are under month-to-month leases with monthly payments of approximately \$900 and \$1,900, respectively.

We believe that our present facilities are adequate to meet our needs and that, if we require additional space, it will be available on commercially reasonable terms.

ITEM 3. 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 4. MINE SAFETY DISCLOSURES

Not applicable.

## PART II

## ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES.

Our common stock has been quoted on the Over the Counter Bulletin Board under the trading symbol PBSV since December 4, 2006. The table below presents the closing high and low bid prices for our common stock for each quarter during the two most recent fiscal years. These prices reflect inter-dealer prices, without retail markup, markdown, or commission, and may not represent actual transactions.

| Quarter Ending   | High Bid | Low Bid |
|------------------|----------|---------|
| October 31, 2013 | \$ 1.65  | \$ 1.30 |
| July 31, 2013    | 1.35     | 0.96    |
| April 30, 2013   | 1.38     | 0.85    |
| January 31, 2013 | 0.90     | 0.70    |
| October 31, 2012 | 0.93     | 0.76    |
| July 31, 2012    | 0.89     | 0.65    |
| April 30, 2012   | 0.90     | 0.64    |
| January 31, 2012 | 0.78     | 0.65    |

On January 24, 2014, the closing price of our common stock on the Over the Counter Bulletin Board was \$2.04 per share and there were approximately 83 holders of record of our common stock.

Prior to the acquisition of Pharma-PR in 2006, Pharma-PR was taxed as an N Corporation under the Puerto Rico Internal Revenue Code, which is similar to that of an S Corporation under the Internal Revenue Code. As a result, all of the income from Pharma-PR was taxed to our then sole stockholder. Other than the distributions to our then sole stockholder which were made during the period that we were an N Corporation, we have not paid dividends on our common stock. We plan to retain future earnings, if any, for use in our business. We do not anticipate paying dividends on our common stock in the foreseeable future.

As of October 31, 2013 and 2012, the Company has not recognized deferred income taxes on \$14.4 million and \$10.5 million of undistributed earnings of its Puerto Rican subsidiaries, respectively, 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 Puerto Rico earnings distribution tax and United States federal income tax for the aggregate amount of approximately \$2.9 million and \$1.6 million at October 31, 2013 and 2012, respectively.

## Equity Compensation Plan Information

The following table summarizes the equity compensation plans under which our securities may be issued as of October 31, 2013.

| Plan Category  | Number of securities to be issued upon exercise of outstanding options | Weighted-average exercise price per share of outstanding options and warrants | Number of securities remaining available for future issuance under equity compensation plans |
|--|--|---|--|
| Equity compensation plans approved by security holders | 1,170,000  | \$ 0.6831   | 1,330,000  |

|   |      |        |        |
|---|------|--------|--------|
| Equity compensation plan not approved by security holders | - \$ | 0.0600 | 16,500 |
|---|------|--------|--------|

The securities issuable pursuant to the equity plan that was approved by security holders, are issuable in accordance with the 2005 long-term incentive plan. The plan was approved by stockholders in April 2006, and amended by stockholder approval in April 2007.

The equity compensation plan not approved by security holders pertain to approximately 16,500 shares of common stock underlying options issuable to employees.

#### Sales of Unregistered Securities

On January 13, 2014 and January 15, 2014, eight warrant holders exercised their warrants to purchase an aggregate of 240,800 shares of common stock of the Company at an exercise price of \$.06 per share (the "Warrants"). The Warrants issued in 2004 were exercised on a cashless basis and, as a result, the Company issued an aggregate of 233,763 shares of common stock of the Company. The issuance of the shares of common stock upon the exercise of the Warrants is exempt from the registration requirements of the Securities Act of 1933, as amended (the "Act"), in accordance with Section 4(2) of the Act, as a transaction by an issuer not involving any public offering.

## ITEM 6. SELECTED FINANCIAL DATA.

Not Applicable.

## ITEM 7. 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 Part I, including matters set forth in the "Risk Factors" section of this Annual Report on Form 10-K, and our Consolidated Financial Statements and notes thereto included elsewhere in this Annual Report on Form 10-K.

### Overview

We are a compliance, project management and technology transfer support consulting firm with a laboratory testing facility 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, 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 also provide microbiological testing services and chemical testing services through our laboratory testing facility ("Lab") in Puerto Rico. We also provide information technology consulting services and technical training/seminars, which services are not currently significant to our operating results. We market our services to pharmaceutical, chemical, biotechnology and medical devices, and allied products companies in Puerto Rico, the United States and Europe. Our team includes more than 300 experienced engineering and life science professionals, and includes former quality assurance managers and directors, and experienced and trained professionals with bachelors, masters and doctorate degrees in health sciences and engineering.

We actively operate in Puerto Rico, the United States, Ireland and Spain and pursue to further expand these markets by strengthening our business development infrastructure and by constantly realigning our business strategies as new opportunities and challenges arise.

We market 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, our portfolio of services include a laboratory testing facility, an information technology consulting practice and a training center that provides seminars/training to the industry.

The Lab incorporates the latest technology and test methodologies meeting pharmacopoeia industry standards and regulations. It currently offers services to our core industries already serviced as well as the cosmetic and food industries.

We also provide technical seminars/training that incorporate the latest regulatory trends and standards as well as other related areas. A network of leading industry professional experts in their field, which include resources of our own, provide these seminars/training to the industry through our "Pharma Serv Academy" division. These services are

provided in the markets we currently serve, as well as others, and position our Company as a key leader in the industry.

Our information technology services and consulting division based in Puerto Rico (“Integratek”) provide 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.

In line with the strategy to further penetrate the United States and Puerto Rico markets, we submit annually for renewal the certification as a "minority-controlled company" as defined by the National Minority Supplier Development Council and Growth Initiative ("NMSDC"). This certification allows us to participate in corporate diversity programs available from various potential customers in the United States and Puerto Rico.

In June 2011, Pharma-Bio, Pharma-PR and Pharma-Serv obtained a new Grant of Industrial Tax Exemption pursuant to the terms and conditions set forth in Act No. 73 of May 28, 2008 ("the Grant") issued by the Puerto Rico Industrial Development Company ("PRIDCO"). The Grant provides relief on various Puerto Rico taxes, including income tax, with certain limitations for most of the activities carried on within Puerto Rico, including those that are for services to parties located outside of Puerto Rico.

Industry consolidations, the pharmaceutical regulatory environment, changes in tax laws, customers' price sensitive procurement processes, and the local and global economies recession continue to be factors and uncertainties that affect our business. As such, we are constantly realigning our business strategies as new opportunities and challenges arise.

For the year ended October 31, 2013, the Company increased its net revenues by \$3.8 million, or 13%, when compared to the same period last year. The United States consulting market division and the Lab led the revenue improvement for the year ended October 31, 2013 with an increase in revenues of \$2.2 and \$1.0 million, respectively, when compared to the same period last year. Other company divisions sustained minor revenue gains/losses or remained constant, when compared to the same period last year. Business development and operations support expenses in the United States and Puerto Rico markets were increased to follow the consulting business favorable revenue trend of last fiscal year. In addition, we have made business development investments in Spain to diversify our European division market, and also continue our efforts to broaden the Lab's customer base.

The revenue growth, offset by the increase in operational support and business development expenses, has led our year ended October 31, 2013 net income to be approximately \$4.9 million, an increase of approximately \$0.2 million, when compared with the same period last year.

The following table sets forth information as to our revenue for the years ended October 31, 2013 and 2012, by geographic regions (dollars in thousands).

| Revenues by Region | Year ended October 31, |        |           |        |
|--------------------|------------------------|--------|-----------|--------|
|                    | 2013                   |        | 2012      |        |
| Puerto Rico        | \$ 17,973              | 54.4%  | \$ 16,856 | 57.7%  |
| United States      | 11,492                 | 34.7%  | 9,159     | 31.3%  |
| Europe             | 3,597                  | 10.9%  | 3,212     | 11.0%  |
|                    | \$ 33,062              | 100.0% | \$ 29,227 | 100.0% |

Weak economies where we do business and worldwide industry consolidations will continue to be unfavorable factors going forward. These factors, and the impact on the industry, if any, of the recently enacted U.S. health care reform (Patient Protection and Affordable Care Act) and Puerto Rico Act 154 which imposed temporary excise taxes to the industry we serve, remain as industry uncertainties that might adversely affect our future performance. We believe that our future profitability and liquidity will be highly dependent on the effect the global economy, changes in tax laws and worldwide lifescience manufacturing 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 years ended October 31, 2013 and 2012, (dollars in thousands) and as a percentage of revenue:

|  | Year ended October 31, |         |           |         |
|--|------------------------|---------|-----------|---------|
|  | 2013                   |         | 2012      |         |
| Revenues                                     | \$ 33,062              | 100.0 % | \$ 29,227 | 100.0 % |
| Cost of services                             | 21,229                 | 64.2 %  | 19,355    | 66.2 %  |
| Gross profit                                 | 11,833                 | 35.8 %  | 9,872     | 33.8 %  |
| Selling, general and administrative expenses | 5,761                  | 17.4 %  | 4,138     | 14.2 %  |
| Other income, net                            | 4                      | 0.0%    | 22        | 0.1 %   |
| Income before income taxes                   | 6,076                  | 18.4 %  | 5,756     | 19.7 %  |
| Income tax expense                           | 1,170                  | 3.6 %   | 1,069     | 3.7 %   |
| Net income                                   | 4,906                  | 14.8 %  | 4,687     | 16.0 %  |

Revenues. Revenues for the year ended October 31, 2013 were \$33.1 million, an increase of approximately \$3.8 million, or 13%, when compared to last year. This improvement is mainly attributable to \$2.2 and \$1.0 million gain in the United States consulting market and Lab services, respectively, plus other minor revenue gains from other Company divisions, offset by a decrease in revenues in the Integratek division of \$0.4 million.

During the year ended October 31, 2013, the United States consulting operation has been able to capture and maintain projects within existing customers, while the Lab has attracted some additional customers that brought non-recurring volume. Integratek has been affected by the loss of volume of one of its major customers. A significant portion of the revenues for the European market is mostly attributable to one customer located in Ireland.

Cost of Services; gross profit. The overall gross profit for the year ended in October 31, 2013 reflected a gross profit net improvement of 2.0 percentage points, when compared to last year.

The Company's net increase in gross margin is mainly attributable to gains in the Lab gross margin of 1.4 percentage points, while consulting services accounted for the remaining net gross margin improvement. The favorable Lab contribution to gross margin is attributable to the favorable yield attained in the Lab due to the increase in testing volume, versus the absorption of fixed cost of services.

Selling, General and Administrative Expenses. Selling, general and administrative expenses for the year ended in October 31, 2013 were approximately \$5.7 million, a net increase in expenses of approximately \$1.6 million as compared to last year.

Business development and operations support expenses in the Puerto Rico and United States markets were increased to follow the consulting business favorable revenue trend. We have also made business development investments in Spain to diversify our European division market.

Income Taxes Expense. The favorable variance in the effective income tax rate from the statutory rate is attributable to the effect of the Puerto Rico Act 73 Tax Grant over income tax expense. For the year ended October 31, 2013, the effective income tax rate increased when compared to the same period last year by 0.7 percentage points. The increase is mainly attributable to the United States segment increase in income before tax, which is taxed at a rate higher than nondomestic jurisdictions.

Net Income. Our net income for year ended October 31, 2013 was approximately \$4.9 million, an increase of \$0.2 million, or an increase of 4.7%, when compared to last year.

For the year ended October 31, 2013, earnings per common share basic and diluted were \$0.221 and \$0.207, respectively, a common share basic decrease of \$0.005 and common share diluted increase of \$0.003, when compared to last year. The decrease is primarily attributable to an increased number of shares outstanding.

Our net income improvement is attributable mainly to the increase in overall gross profit, the savings obtained by the Grant, offset by the increase in selling general and administrative expenses to support the favorable revenue trend.

## Liquidity and Capital Resources

Liquidity is a measure of our ability to meet potential cash requirements, including planned capital expenditures. For the year ended October 31, 2013, we generated a working capital increase of approximately \$5.3 million.

Our primary cash needs consist of the payment of compensation to our professional staff, overhead expenses, and statutory taxes. Management believes that based on the current level of operations and cash flows from operations, the collectibility of high quality customer receivables will be sufficient to fund anticipated expenses and satisfy other possible long-term contractual commitments for the next twelve months.

To the extent that we pursue possible opportunities 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.

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, as described above, management is not aware of any trends or events likely to have a material adverse effect on liquidity or its financial statements.

## Off-Balance Sheet Arrangements

We were not involved in any significant off-balance sheet arrangements during the fiscal year ended October 31, 2013.

## Critical Accounting Policies and Estimates

The discussion and analysis of our financial condition and results of operations are based upon our consolidated financial statements, which have been prepared in accordance with generally accepted accounting principles (“GAAP”) in the United States. We believe the following are the critical accounting policies that impact the consolidated financial statements, some of which are based on management’s best estimates available at the time of preparation. Actual experience may differ from these estimates.

**Consolidation** - The accompanying consolidated financial statements include the accounts of all of our wholly 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 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** - Accounting standards have established a fair value hierarchy that requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. A financial instrument’s categorization within the fair value hierarchy is based upon the lowest level of input that is significant to the fair value measurement. Accounting standards have established three levels of inputs that may be used to measure fair value:

Level 1: Quoted prices in active markets for identical assets and liabilities.

Level 2: Observable inputs other than Level 1 prices such as quoted prices for similar assets or liabilities, quoted prices in markets with insufficient volume or infrequent transactions (less active markets), or model-derived valuations in which all significant inputs are observable or can be derived principally from or corroborated by observable market data for substantially the full term of the assets or liabilities.

Level 3: Prices or valuation techniques that require inputs that are both significant to the fair value measurement and unobservable (supported by little or no market activity).

Marketable securities available-for-sale consist of U.S. Treasury securities and an obligation from the Puerto Rico Government Development Bank valued using quoted market prices in active markets. Accordingly, these securities are categorized in Level 1.

The carrying value of the Company's financial instruments (excluding marketable securities and obligations under capital leases), 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 approximates the carrying amount.

**Revenue Recognition** - Revenue is primarily derived from: (1) time and materials contracts (representing approximately 92% of total revenues), which is recognized by applying the proportional performance model, whereby revenue is recognized as performance occurs, (2) short-term fixed-fee contracts or "not to exceed" contracts (representing approximately 2% of total revenues), which revenue is recognized similarly, except that certain milestones also have to be reached before revenue is recognized, and (3) laboratory testing revenue (representing approximately 6% of total revenues) which is mainly recognized as the testing is completed and certified (normally within days of sample receipt from customer). If we determine that a contract will result in a loss, we recognize 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.

**Marketable Securities** - We consider our marketable security investment portfolio and marketable equity investments available-for-sale and, accordingly, these investments are recorded at fair value with unrealized gains and losses generally recorded in other comprehensive income; whereas realized gains and losses are included in earnings and determined based on the specific identification method.

**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. Our 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 our customers, bad debts are mainly 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** - We follow 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.

The Company follows guidance from the Financial Accounting Standards Board ("FASB") related to Accounting for Uncertainty in Income Taxes, which includes a two-step approach to recognizing, de-recognizing and measuring uncertain tax positions. As of October 31, 2013, the Company had no significant uncertain tax positions that would be reduced as a result of a lapse of the applicable statute of limitations.

**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 amounts 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 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.

We evaluate for impairment our 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.

**Stock-based Compensation** - Stock-based compensation expense is recognized in the consolidated financial statements based on the fair value of the awards granted. 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. We calculate the fair value of stock options using the Black-Scholes option-pricing model at grant date. Excess tax benefits related to stock-based compensation are reflected as cash flows from financing activities rather than cash flows from operating activities. We have not recognized 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 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. 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 our foreign subsidiary is its local currency. The assets and liabilities of our 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.

Our intercompany accounts are typically denominated in the functional currency of the foreign subsidiary. Gains and losses resulting from the remeasurement of intercompany receivables that we consider 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 we anticipate 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.

#### New Accounting Standards

Recently issued FASB guidance and Securities Exchange Commission Staff Accounting Bulletins have either been implemented, with no significant effect, or are not applicable to the Company.

#### 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 Annual Report on Form 10-K, 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 Annual Report on Form 10-K 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 any changes in that industry or in the markets we serve could impair our ability to generate revenue and realize a profit.

Puerto Rico government enacted ACT 154 of October 22, 2010 which may affect adversely the willingness of our customers to do business in Puerto Rico and consequently affect our business.

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, or may also consider closing operations carried in Puerto Rico.

Other factors, including economic factors, may affect the decision of businesses to continue or expand their operations in the markets we serve.

Our business and operating results may be impacted if we are unable to maintain our certification as a minority-controlled company.

Because our business is dependent upon a small number of clients, the loss of a major client could impair our ability to operate profitably.

Customer procurement and sourcing practices intended to reduce costs could have an adverse affect on our margins and profitability.

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.

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.

Our reputation and divisions may be impacted by regulatory standards impacting our customer products.



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, the United States, Ireland and Spain.

Our cash could be adversely affected if the financial institutions in which we hold our cash fail.

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 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 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 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURE ABOUT MARKET RISK.

Not applicable.

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA.

Our Consolidated Financial Statements, together with the report of our independent registered public accounting firm are included herein immediately following the signature page of this report. See Index to Consolidated Financial Statements on page F-1.

ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE.

None.

ITEM 9A. CONTROLS AND PROCEDURES.

Management's Annual Report on Internal Control Over Financial Reporting

Our management is responsible for establishing and maintaining adequate "internal control over financial reporting," as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act, for the Company. This rule defines internal control over financial reporting as a process designed by, or under the supervision of, a company's principal executive officer and principal financial officer, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. Our internal control over financial reporting includes those policies and procedures that:

pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company;

provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and

provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, our internal control systems and procedures may not prevent or detect misstatements. An internal control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, have been detected. Also, projections of any evaluation of effectiveness to future periods are subject to the risks that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies and procedures may deteriorate.

We, under the supervision of and with the participation of our management, including the principal executive officer and principal financial officer, assessed the effectiveness of the Company's internal control over financial reporting as of October 31, 2013, based on criteria for effective internal control over financial reporting described in "Internal Control — Integrated Framework" issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on this assessment, our principal executive officer and principal financial officer concluded that the Company maintained effective internal control over financial reporting as of October 31, 2013, based on the specified criteria.

#### Disclosure Controls and Procedures.

We carried out an evaluation, under the supervision and with the participation of our management, including our principal executive officer and principal 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 Annual Report. Based upon that evaluation, our principal executive officer and principal financial officer concluded that our disclosure controls and procedures were effective as of the end of the period covered by this Annual 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.

#### ITEM 9B. OTHER INFORMATION.

None.

PART III

ITEM 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE.

The information required by this Item is incorporated by reference to our Proxy Statement for our Annual Meeting of Stockholders for the fiscal year ended October 31, 2013, which will be filed with Securities and Exchange Commission no later than 120 days after the end of the fiscal year covered by this Form 10-K, or, alternatively, by amendment to this Form 10-K under cover of Form 10-K/A no later than the end of such 120 day period.

Information with respect to our executive officers is included in Part I.

ITEM 11. EXECUTIVE COMPENSATION.

The information required by this Item is incorporated by reference to our Proxy Statement for our Annual Meeting of Stockholders for the fiscal year ended October 31, 2013, which will be filed with Securities and Exchange Commission no later than 120 days after the end of the fiscal year covered by this Form 10-K, or, alternatively, by amendment to this Form 10-K under cover of Form 10-K/A no later than the end of such 120 day period.

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS.

The information required by this Item is incorporated by reference to our Proxy Statement for our Annual Meeting of Stockholders for the fiscal year ended October 31, 2013, which will be filed with Securities and Exchange Commission no later than 120 days after the end of the fiscal year covered by this Form 10-K, or, alternatively, by amendment to this Form 10-K under cover of Form 10-K/A no later than the end of such 120 day period.

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS, AND DIRECTOR INDEPENDENCE.

The information required by this Item is incorporated by reference to our Proxy Statement for our Annual Meeting of Stockholders for the fiscal year ended October 31, 2013, which will be filed with Securities and Exchange Commission no later than 120 days after the end of the fiscal year covered by this Form 10-K, or, alternatively, by amendment to this Form 10-K under cover of Form 10-K/A no later than the end of such 120 day period.

ITEM 14. PRINCIPAL ACCOUNTING FEES AND SERVICES.

The information required by this Item is incorporated by reference to our Proxy Statement for our Annual Meeting of Stockholders for the fiscal year ended October 31, 2013, which will be filed with Securities and Exchange Commission no later than 120 days after the end of the fiscal year covered by this Form 10-K, or, alternatively, by amendment to this Form 10-K under cover of Form 10-K/A no later than the end of such 120 day period.

## PART IV

## ITEM 15. EXHIBITS, FINANCIAL STATEMENT SCHEDULES.

The following documents are filed as a part of this Annual Report on Form 10-K:

1. All Financial Statements: Consolidated Financial Statements are included herein immediately following the signature page of this report. See Index to Consolidated Financial Statements on page F-1.
2. Financial Statement Schedules: None.
3. Exhibits: The following exhibits are filed herewith or are incorporated by reference to exhibits previously filed with the Commission, as indicated in the description of each.

| Exhibit Number | Exhibit Description  | Form     | File Number | Incorporated By Reference |             |
|----------------|--|----------|-------------|---------------------------|-------------|
|                |  |          |             | Exhibit                   | Filing Date |
| 3.1            | Restated Certificate of Incorporation  | 8-K      | 000-50956   | 99.1                      | 5/1/2006    |
| 3.2            | Certificate of Amendment to the Certificate of Incorporation   | 8-K      | 000-50956   | 3.1                       | 4/12/13     |
| 3.3            | By-laws  | 10-SB12G | 000-50956   | 3.2                       | 9/24/2004   |
| 3.4            | Amendment No. 1 to the By-laws   | 8-K      | 000-50956   | 3.1                       | 6/6/2008    |
| 3.5            | Amendment No. 2 to the By-laws   | 8-K      | 000-50956   | 3.2                       | 4/12/13     |
| 4.1            | Form of warrant issued to Investors in January 2006 private placement                                    | 8-K      | 000-50956   | 4.2                       | 1/31/2006   |
| 4.2            | Form of warrant held by initial warrant holders  | 8-K      | 000-50956   | 4.3                       | 1/31/2006   |
| 4.3            | Form of warrant held by San Juan Holdings  | 8-K      | 000-50956   | 4.4                       | 1/31/2006   |
| 4.4            | Form of warrants issued to broker-dealers in January 2006 private placement                              | 8-K      | 000-50956   | 4.5                       | 1/31/2006   |
| 4.5            | Form of First Amendment to Series C Common Stock Purchase Warrant.                                       | 8-K      | 000-50956   | 4.1                       | 1/29/2009   |
| 10.1           | Form of subscription agreement for January 2006 private placement  | 8-K      | 000-50956   | 99.1                      | 1/31/2006   |
| 10.2           | Registration rights provisions for the subscription agreement relating to January 2006 private placement | 8-K      | 000-50956   | 99.2                      | 1/31/2006   |
| 10.3           | Registration rights provisions for Elizabeth Plaza and San Juan  | 8-K      | 000-50956   | 99.3                      | 1/31/2006   |

Edgar Filing: Pharma-Bio Serv, Inc. - Form 10-K

| Holdings, Inc. |  |        |           |      |           |
|----------------|--|--------|-----------|------|-----------|
| 10.4           | Employment Agreement dated January 2, 2008 between the Registrant and Elizabeth Plaza                            | 10-KSB | 000-50956 | 10.5 | 1/31/2008 |
| 10.5           | Amendment to Employment Agreement dated June 9, 2008 between the Registrant and Elizabeth Plaza                  | 10-K   | 000-50956 | 10.5 | 1/29/2009 |
| 10.6           | Second Amendment to Employment Agreement, dated March 11, 2009, by and between the Company and Elizabeth Plaza.  | 8-K    | 000-50956 | 10.1 | 3/17/2009 |
| 10.7           | Third Amendment to Employment Agreement, dated March 11, 2009, by and between the Company and Elizabeth Plaza.   | 8-K    | 000-50956 | 10.2 | 3/17/2009 |
| 10.8           | Employment Agreement Amendment, effective as of January 1, 2010, by and between the Company and Elizabeth Plaza. | 8-K    | 000-50956 | 10.1 | 1/07/2010 |

Edgar Filing: Pharma-Bio Serv, Inc. - Form 10-K

|       |   |         |            |            |            |
|-------|---|---------|------------|------------|------------|
| 10.9  | Employment Agreement Amendment, effective as of July 1, 2010, by and between the Company and Elizabeth Plaza          | 8-K     | 000-50956  | 10.1       | 7/8/2010   |
| 10.10 | Sixth Employment Agreement Amendment, effective as of August 23, 2010, by and between the Company and Elizabeth Plaza | 8-K     | 000-50956  | 10.1       | 8/27/10    |
| 10.11 | Employment Agreement dated January 25, 2006 between the Registrant and Nélica Plaza                                   | 8-K     | 000-50956  | 99.5       | 1/31/2006  |
| 10.12 | Amendment to Employment Agreement, dated March 11, 2009, by and between the Company and Nélica Plaza.                 | 8-K     | 000-50956  | 10.4       | 3/17/2009  |
| 10.13 | Employment Agreement, dated as of December 31, 2009, by and between Pharma-Bio Serv PR, Inc. and Nélica Plaza.        | 8-K     | 000-50956  | 10.3       | 1/07/2010  |
| 10.14 | Employment Agreement dated November 5, 2007 between the Registrant and Pedro Lasanta                                  | 10-K    | 000-50956  | 10.8       | 1/29/2009  |
| 10.15 | Amendment to Employment Agreement dated December 17, 2008 between the Registrant and Pedro Lasanta                    | 8-K     | 000-50956  | 99.1       | 12/23/2008 |
| 10.16 | Amendment to Employment Agreement, dated March 11, 2009, by and between the Company and Pedro Lasanta.                | 8-K     | 000-50956  | 10.3       | 3/17/2009  |
| 10.17 | Employment Agreement Amendment, effective as of January 1, 2010, by and between the Company and Pedro Lasanta.        | 8-K     | 000-50956  | 10.2       | 1/07/2010  |
| 10.18 | 2005 Long-term incentive plan, as amended   | DEF 14A | 000-50956  | Appendix C | 3/26/2007  |
| 10.19 | Lease dated March 16, 2004 between Plaza Professional Center, Inc. and the Registrant                                 | SB-2    | 333-132847 | 10.9       | 3/30/2006  |

Edgar Filing: Pharma-Bio Serv, Inc. - Form 10-K

|       |  |      |            |       |           |
|-------|--|------|------------|-------|-----------|
| 10.20 | Lease dated November 1, 2004<br>between Plaza Professional Center,<br>Inc. and the Registrant  | SB-2 | 333-132847 | 10.10 | 3/30/2006 |
| 10.21 | Seventh Employment Agreement<br>Amendment, dated January 23, 2012<br>and effective as of January 1, 2012, by<br>and between the Company and<br>Elizabeth Plaza | 8-K  | 000-50956  | 99.1  | 1/23/2012 |



Edgar Filing: Pharma-Bio Serv, Inc. - Form 10-K

|       |  |        |           |      |           |
|-------|--|--------|-----------|------|-----------|
| 10.22 | Employment Agreement Amendment, dated January 31, 2012, by and between the Company and Pedro J. Lasanta  | 8-K    | 000-50956 | 10.1 | 2/2/2012  |
| 10.23 | Employment Agreement Amendment, dated December 31, 2012, by and between the Company and Pedro J. Lasanta   | 8-K    | 000-50956 | 10.1 | 1/7/2013  |
| 10.24 | Consulting Agreement, dated January 7, 2013, by and between Pharma-Bio Serv, Inc. and Elizabeth Plaza  | 8-K    | 000-50956 | 10.1 | 1/11/2013 |
| 10.25 | Employment Agreement Amendment, dated January 7, 2013, by and among Pharma-Bio Serv, Inc., Pharma-Bio Serv PR, Inc. and Nélide Plaza   | 8-K    | 000-50956 | 10.2 | 1/11/2013 |
| 10.26 | Employment Agreement Amendment, dated December 31, 2012, by and between the Company and Pedro Lasanta  | 8-K    | 000-50956 | 10.1 | 1/7/13    |
| 10.27 | Consulting Agreement, dated January 7, 2013, by and between the Company and Elizabeth Plaza  | 8-K    | 000-50956 | 10.1 | 1/11/13   |
| 10.28 | Employment Agreement Amendment, dated January 7, 2013, by and among the Company, Pharma-Bio Serv PR, Inc. and Nelida Plaza   | 8-K    | 000-50956 | 10.2 | 1/11/13   |
| 10.29 | Approval of Compensation Committee, dated July 17, 2013, to increase the hours of service pursuant to the Consulting Agreement between the Company and Elizabeth Plaza (a description of such approval was included in the Company's Current Report on Form 8-K, filed with the SEC on July 23, 2013, and incorporated herein by reference). | 8-K    | 000-50956 | -    | 7/23/13   |
| 10.30 | Consulting Agreement, effective January 1, 2014, between Pharma-Bio Serv Inc., Strategic Consultants International, LLC and Elizabeth Plaza.   | 8-K    | 000-50956 | 10.1 | 12/31/13  |
| 14.1  | Code of business conduct and ethics for senior management  | 10-KSB | 000-50956 | 14.1 | 2/2/2007  |
| 21.1* | List of Subsidiaries   |        |           |      |           |
| 23.1* | Consent of Horwath Vélez & Co, PSC   |        |           |      |           |
| 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 chief executive officer and chief financial officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 |
| 101.INS | XBRL Instance Document   |
| 101.SCH | XBRL Taxonomy Extension Schema   |
| 101.CAL | XBRL Taxonomy Extension Calculation Linkbase   |
| 101.DEF | XBRL Taxonomy Extension Definition Linkbase  |
| 101.LAB | XBRL Taxonomy Extension Label Linkbase   |
| 101.PRE | XBRL Taxonomy Extension Presentation Linkbase  |

---

\* Filed herewith

\*\* Furnished herewith

Exhibits 10.4 through 10.18 and 10.21 through 10.30 are management contracts or compensatory plans, contracts or arrangements.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) 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.

Dated : January 29, 2014

By: /s/ Elizabeth Plaza  
 Name: Elizabeth Plaza  
 Title: Chairman  
 (Principal Executive Officer)

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

| Signature                                | Title   | Date             |
|--|---|------------------|
| /s/ Elizabeth Plaza<br>Elizabeth Plaza   | Chairman<br>(Principal Executive Officer)   | January 29, 2014 |
| /s/ Pedro J. Lasanta<br>Pedro J. Lasanta | Chief Financial Officer and Vice<br>President - Finance and Administration<br>(Principal Financial and Accounting<br>Officer) | January 29, 2014 |
| /s/ Kirk Michel<br>Kirk Michel           | Director  | January 29, 2014 |
| /s/ Howard Spindel<br>Howard Spindel     | Director  | January 29, 2014 |
| /s/ Dov Perlysky<br>Dov Perlysky         | Director  | January 29, 2014 |
| /s/ Irving Wiesen<br>Irving Wiesen       | Director  | January 29, 2014 |



PHARMA-BIO SERV, INC.

INDEX TO CONSOLIDATED FINANCIAL STATEMENTS

|  | Page |
|--|------|
| Report of Independent Registered Public Accounting Firm  | F-2  |
| Consolidated Balance Sheets as of October 31, 2013 and 2012  | F-3  |
| Consolidated Statements of Income for the Years Ended October 31, 2013 and 2012                          | F-4  |
| Consolidated Statements of Comprehensive Income for the Years Ended October 31, 2013 and 2012            | F-5  |
| Consolidated Statements of Changes in Stockholders' Equity for the Years Ended October 31, 2013 and 2012 | F-6  |
| Consolidated Statements of Cash Flows for the Years Ended October 31, 2013 and 2012                      | F-7  |
| Notes to Consolidated Financial Statements   | F-8  |

F-1

---

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Stockholders of  
Pharma-Bio Serv, Inc.  
Dorado, Puerto Rico

We have audited the accompanying consolidated balance sheets of Pharma-Bio Serv, Inc. (the "Company") as of October 31, 2013 and 2012, and the related consolidated statements of income, comprehensive income, changes in stockholders' equity, and cash flows for the years then ended. Pharma-Bio Serv, Inc.'s management is responsible for these financial statements. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. Our audit included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Pharma-Bio Serv, Inc. as of October 31, 2013 and 2012, and the consolidated results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

/s/ HORWATH VÉLEZ & CO, PSC  
San Juan, Puerto Rico

January 29, 2014  
Puerto Rico Society of Certified Public Accountants  
Stamp number E95238 was  
affixed to the original of this report

PHARMA-BIO SERV, INC.  
Consolidated Balance Sheets  
October 31, 2013 and 2012

|  | October 31,          |                      |
|--|----------------------|----------------------|
|  | 2013                 | 2012                 |
| <b>ASSETS</b>  |                      |                      |
| <b>Current assets</b>  |                      |                      |
| Cash and cash equivalents  | \$ 12,045,923        | \$ 6,538,113         |
| Marketable securities  | 71,260               | 95,000               |
| Accounts receivable  | 7,403,987            | 7,580,167            |
| Other  | 767,452              | 382,773              |
| <b>Total current assets</b>  | <b>20,288,622</b>    | <b>14,596,053</b>    |
| Property and equipment   | 976,423              | 1,113,371            |
| Other assets   | 16,891               | 25,592               |
| <b>Total assets</b>  | <b>\$ 21,281,936</b> | <b>\$ 15,735,016</b> |
| <b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>  |                      |                      |
| <b>Current liabilities</b>   |                      |                      |
| Current portion-obligations under capital leases   | \$ 32,188            | \$ 39,436            |
| Accounts payable and accrued expenses  | 2,825,532            | 2,562,462            |
| Income taxes payable   | 322,731              | 173,620              |
| <b>Total current liabilities</b>   | <b>3,180,451</b>     | <b>2,775,518</b>     |
| Obligations under capital leases   | 51,724               | 83,912               |
| <b>Total liabilities</b>   | <b>3,232,175</b>     | <b>2,859,430</b>     |
| <b>Stockholders' equity:</b>   |                      |                      |
| 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 22,702,186 and 20,758,695 shares at October 31, 2013 and 2012, respectively | 2,271                | 2,076                |
| Additional paid-in capital   | 931,039              | 678,214              |
| Retained earnings  | 17,193,203           | 12,286,714           |
| Accumulated other comprehensive loss   | (76,752)             | (91,418)             |
| <b>Total stockholders' equity</b>  | <b>18,049,761</b>    | <b>12,875,586</b>    |
| <b>Total liabilities and stockholders' equity</b>  | <b>\$ 21,281,936</b> | <b>\$ 15,735,016</b> |

See notes to consolidated financial statements.

PHARMA-BIO SERV, INC.  
Consolidated Statements of Income  
For the Years Ended October 31, 2013 and 2012

|   | Years ended October 31, |               |
|---|-------------------------|---------------|
|   | 2013                    | 2012          |
| REVENUES  | \$ 33,062,010           | \$ 29,227,167 |
| COST OF SERVICES  | 21,228,554              | 19,355,440    |
| GROSS PROFIT  | 11,833,456              | 9,871,727     |
| SELLING, GENERAL AND<br>ADMINISTRATIVE EXPENSES                   | 5,761,742               | 4,138,111     |
| INCOME FROM OPERATIONS  | 6,071,714               | 5,733,616     |
| OTHER INCOME (EXPENSE):   |                         |               |
| Interest expense  | (7,213)                 | (7,425)       |
| Interest income   | 10,326                  | 11,076        |
| Gain on disposition of property and equipment                     | 1,483                   | 18,345        |
|   | 4,596                   | 21,996        |
| INCOME BEFORE INCOME TAXES  | 6,076,310               | 5,755,612     |
| INCOME TAXES  | 1,169,821               | 1,068,606     |
| NET INCOME  | \$ 4,906,489            | \$ 4,687,006  |
| BASIC EARNINGS PER COMMON SHARE                                   | \$ 0.221                | \$ 0.226      |
| DILUTED EARNINGS PER COMMON SHARE                                 | \$ 0.207                | \$ 0.204      |
| WEIGHTED AVERAGE NUMBER OF COMMON<br>SHARES OUTSTANDING – BASIC   | 22,201,514              | 20,758,695    |
| WEIGHTED AVERAGE NUMBER OF COMMON<br>SHARES OUTSTANDING – DILUTED | 23,660,362              | 22,939,701    |

See notes to consolidated financial statements.



PHARMA-BIO SERV, INC.  
 Consolidated Statements of Comprehensive Income  
 For the Years Ended October 31, 2013 and 2012

|   | Years ended October 31, |              |
|---|-------------------------|--------------|
|   | 2013                    | 2012         |
| NET INCOME  | \$ 4,906,489            | \$ 4,687,006 |
| OTHER COMPREHENSIVE INCOME (LOSS), NET OF RECLASSIFICATION ADJUSTMENTS AND TAXES: |                         |              |
| Foreign currency translation gain (loss)  | 38,406                  | (71,409)     |
| Net unrealized losses on available-for-sale securities                            | (23,740)                | -            |
| TOTAL OTHER COMPREHENSIVE INCOME (LOSS)   | 14,666                  | (71,409)     |
| COMPREHENSIVE INCOME  | \$ 4,921,155            | \$ 4,615,597 |

See notes to consolidated financial statements.

PHARMA-BIO SERV, INC.  
Consolidated Statements of Changes in Stockholders' Equity  
For the Years Ended October 31, 2013 and 2012

|  | Common Stock |          | Preferred Stock |        | Additional | Retained      | Accumulated                       | Total         |
|--|--------------|----------|-----------------|--------|------------|---------------|-----------------------------------|---------------|
|  | Shares       | Amount   | Shares          | Amount | Paid-in    |               | Other                             |               |
|  |              |          |                 |        | Capital    | Earnings      | Comprehensive<br>Income<br>(Loss) |               |
| BALANCE AT<br>OCTOBER 31, 2011   | 20,758,695   | \$ 2,076 | -               | \$ -   | \$ 654,550 | \$ 7,599,708  | \$ (20,009)                       | \$ 8,236,325  |
| STOCK-BASED<br>COMPENSATION  | -            | -        | -               | -      | 23,664     | -             | -                                 | 23,664        |
| NET INCOME   | -            | -        | -               | -      | -          | 4,687,006     | -                                 | 4,687,006     |
| OTHER<br>COMPREHENSIVE<br>LOSS,<br>NET OF TAX  | -            | -        | -               | -      | -          | -             | (71,409)                          | (71,409)      |
| BALANCE AT<br>OCTOBER 31, 2012   | 20,758,695   | 2,076    | -               | -      | 678,214    | 12,286,714    | (91,418)                          | 12,875,586    |
| STOCK-BASED<br>COMPENSATION  | -            | -        | -               | -      | 53,161     | -             | -                                 | 53,161        |
| CONVERSION OF<br>WARRANTS TO<br>SHARES OF<br>COMMON STOCK                                  | 1,830,991    | 183      |                 |        | 109,676    |               |                                   | 109,859       |
| ISSUANCE OF<br>COMMON STOCK<br>PURSUANT TO<br>AGREEMENT<br>WITH INVESTOR<br>RELATIONS FIRM | 112,500      | 12       |                 |        | 89,988     |               |                                   | 90,000        |
| NET INCOME   | -            | -        | -               | -      | -          | 4,906,489     | -                                 | 4,906,489     |
| OTHER<br>COMPREHENSIVE<br>INCOME, NET OF<br>TAX  | -            | -        | -               | -      | -          | -             | 14,666                            | 14,666        |
|  | 22,702,186   | \$ 2,271 | -               | \$ -   | \$ 931,039 | \$ 17,193,203 | \$ (76,752)                       | \$ 18,049,761 |

BALANCE AT  
OCTOBER 31, 2013

See notes to consolidated financial statements.

F-6

---

PHARMA-BIO SERV, INC.  
Consolidated Statements of Cash Flows  
For the Years Ended October 31, 2013 and 2012

|   | Years ended October 31, |                     |
|---|-------------------------|---------------------|
|   | 2013                    | 2012                |
| <b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>  |                         |                     |
| Net income  | \$ 4,906,489            | \$ 4,687,006        |
| Adjustments to reconcile net income to net cash provided by operating activities:   |                         |                     |
| Gain on disposition of property and equipment   | (1,483)                 | (18,345)            |
| Stock-based compensation  | 53,161                  | 23,664              |
| Depreciation and amortization   | 344,520                 | 321,732             |
| Decrease (increase) in accounts receivable  | 428,309                 | (2,735,046)         |
| Increase in other assets  | (383,939)               | (50,486)            |
| Increase in liabilities   | 279,629                 | 230,541             |
| <b>NET CASH PROVIDED BY OPERATING ACTIVITIES</b>  | <b>5,626,686</b>        | <b>2,459,066</b>    |
| <b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>  |                         |                     |
| Acquisition of property and equipment   | (219,352)               | (187,362)           |
| Proceeds from disposition of property and equipment   | 13,946                  | 18,836              |
| <b>NET CASH USED IN INVESTING ACTIVITIES</b>  | <b>(205,406)</b>        | <b>(168,526)</b>    |
| <b>CASH FLOW FROM FINANCING ACTIVITIES:</b>   |                         |                     |
| Proceeds from issuance of common stock  | 109,859                 | -                   |
| Payments on obligations under capital lease   | (39,436)                | (32,826)            |
| <b>NET CASH USED IN FINANCING ACTIVITIES</b>  | <b>70,423</b>           | <b>(32,826)</b>     |
| <b>EFFECT OF EXCHANGE RATE CHANGES ON CASH</b>  | <b>16,107</b>           | <b>(36,326)</b>     |
| <b>NET INCREASE IN CASH AND CASH EQUIVALENTS</b>  | <b>5,507,810</b>        | <b>2,221,388</b>    |
| <b>CASH AND CASH EQUIVALENTS - BEGINNING OF YEAR</b>  | <b>6,538,113</b>        | <b>4,316,725</b>    |
| <b>CASH AND CASH EQUIVALENTS – END OF YEAR</b>  | <b>\$ 12,045,923</b>    | <b>\$ 6,538,113</b> |
| <b>SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:</b>   |                         |                     |
| Cash paid during the period for:  |                         |                     |
| Income taxes  | \$ 1,325,910            | \$ 1,543,021        |
| Interest  | \$ 7,213                | \$ 7,425            |
| <b>SUPPLEMENTARY SCHEDULES OF NON-CASH INVESTING AND FINANCING ACTIVITIES:</b>  |                         |                     |
| Property and equipment with accumulated depreciation of \$4,532 and \$32,122 disposed during the years ended October 31, 2013 and 2012, respectively. | \$ 16,995               | \$ 32,613           |
| Income tax withheld by clients to be used as a credit in the Company's income tax returns   | \$ 204,325              | \$ 39,120           |
| Issuance of common stock pursuant to agreement with investor relations firm   | \$ 90,000               | \$ -                |
| Obligations under capital lease incurred for the acquisition of a vehicle   | \$ -                    | \$ 32,795           |

See notes to consolidated financial statements.

PHARMA-BIO SERV, INC.  
Notes To Consolidated Financial Statements  
For the Years Ended October 31, 2013 and 2012

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”), Pharma Serv, Inc. (“Pharma-Serv”) both Puerto Rico corporations, Pharma-Bio Serv US, Inc. (“Pharma-US”), a Delaware corporation, Pharma-Bio Serv Validation & Compliance Limited (“Pharma-IR”), an Irish corporation, and Pharma-Bio Serv SL (“Pharma-Spain”) a Spanish limited liability company. Pharma-Bio, Pharma-PR, Pharma-Serv, Pharma-US, Pharma-IR and Pharma-Spain are collectively referred to as the “Company.” The Company operates in Puerto Rico, the United States, Ireland and Spain under the name of Pharma-Bio Serv and is engaged in providing technical compliance consulting service, and microbiological and chemical laboratory testing services primarily to the pharmaceutical, chemical, medical device and biotechnology industries.

Pharma-Spain is a wholly owned subsidiary, which started operations in January 2013.

SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Consolidation

The accompanying consolidated financial statements include the accounts of the Company and all of its wholly 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

Accounting standards have established a fair value hierarchy that requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. A financial instrument’s categorization within the fair value hierarchy is based upon the lowest level of input that is significant to the fair value measurement. Accounting standards have established three levels of inputs that may be used to measure fair value:

Level 1: Quoted prices in active markets for identical assets and liabilities.

Observable inputs other than Level 1 prices such as quoted prices for similar assets or  
Level 2: liabilities, quoted prices in markets with insufficient volume or infrequent transactions (less active markets), or model-derived valuations in which all significant inputs are observable or can be derived principally from or corroborated by observable market data for substantially the full term of the assets or liabilities.

Prices or valuation techniques that require inputs that are both significant to the fair value Level 3: measurement and unobservable (supported by little or no market activity).

Marketable securities available-for-sale consist of U.S. Treasury securities and an obligation from the Puerto Rico Government Development Bank valued using quoted market prices in active markets. Accordingly, these securities are categorized in Level 1.

The carrying value of the Company's financial instruments (excluding marketable securities and obligations under capital leases): 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 approximates the carrying amount.

F-8

---

## Revenue Recognition

Revenue is primarily derived from: (1) time and materials contracts (representing approximately 92% of total revenues), which is recognized by applying the proportional performance model, whereby revenue is recognized as performance occurs, (2) short-term fixed-fee contracts or "not to exceed" contracts (representing approximately 2% of total revenues), which revenue is recognized similarly, except that certain milestones also have to be reached before revenue is recognized, and (3) laboratory testing revenue (representing approximately 6% of total revenues), which is mainly recognized as the testing is completed and certified (normally within days of sample receipt from customer). If the Company determines that a 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 money market obligation's trusts that are registered under the U.S. Investment Company Act of 1940 and liquid investments with original maturities of three months or less.

## Marketable Securities

We consider our marketable security investment portfolio and marketable equity investments as available-for-sale and, accordingly, these investments are recorded at fair value with unrealized gains and losses generally recorded in other comprehensive income; whereas realized gains and losses are included in earnings and determined based on the specific identification method.

## 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 mainly 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 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.

The Company follows guidance from the Financial Accounting Standards Board ("FASB") related to Accounting for Uncertainty in Income Taxes, which includes a two-step approach to recognizing, de-recognizing and measuring uncertain tax positions. As of October 31, 2013, the Company had no significant uncertain tax positions that would be reduced as a result of a lapse of the applicable statute of limitations.

## 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.

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.

#### Stock-based Compensation

Stock-based compensation expense is recognized in the consolidated financial statements based on the fair value of the awards granted. 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. Excess tax benefits related to stock-based compensation are reflected as cash flows from financing activities rather than cash flows from operating activities. The Company has not recognized 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 subsidiaries are its local currency. The assets and liabilities of the Company's foreign subsidiaries 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.

### Subsequent Events

The Company has evaluated subsequent events to the date of the audit report as of January 29, 2014.

The Company has determined that there are no events occurring in this period that required disclosure in or adjustment except as disclosed in the accompanying consolidated financial statements.

### Reclassifications

Certain reclassifications have been made to the October 31, 2012 consolidated financial statements to conform them to the October 31, 2013 consolidated financial statements presentation. Such reclassifications do not have effect on net income as previously reported.

### Recent Accounting Pronouncements

Recent issued FASB guidance and Securities and Exchange Commission ("SEC") Staff Accounting Bulletins have either been implemented, with no significant effect, or are not applicable to the Company.

## NOTE B – MARKETABLE SECURITIES AVAILABLE FOR SALE

The amortized cost, gross unrealized gains, gross unrealized losses and estimated fair values of available-for-sale securities by type of security were as follows as of October 31, 2013:

| Type of security as of October 31, 2013                  | Amortized<br>Cost | Gross<br>Unrealized<br>Gains | Gross<br>Unrealized<br>Losses | Estimated<br>Fair Value |
|--|-------------------|------------------------------|-------------------------------|-------------------------|
| U.S. Treasury securities                                 | \$4,500,000       | \$—                          | \$—                           | \$4,500,000             |
| Other government-related debt securities:                |                   |                              |                               |                         |
| Puerto Rico Commonwealth Government Development<br>Bond  | 95,000            | —                            | (23,740 )                     | 71,260                  |
| Total interest-bearing and available-for-sale securities | \$4,595,000       | \$—                          | \$(23,740 )                   | \$4,571,260             |

At October 31, 2013 and 2012, the above marketable securities included a \$95,000 5.4% Puerto Rico Commonwealth Government Development Bank Bond, purchased at par and maturing in August 2019. As of October 31, 2012, this bond was the only marketable security investment, and its balance approximated its fair market value, therefore no realized or unrealized gains or losses were recorded then.

The fair values of available-for-sale securities by classification in the Consolidated Balance Sheets were as follows as of October 31, 2013 and 2012:

| Classification in the Consolidated Balance Sheets | 2013        | 2012     |
|---|-------------|----------|
| Cash and cash equivalents                         | \$4,500,000 | \$—      |
| Marketable securities                             | 71,260      | 95,000   |
| Total available-for-sale securities               | \$4,571,260 | \$95,000 |

Cash and cash equivalents in the table above exclude cash in banks of approximately \$7.5 million as of October 31, 2013.

The primary objectives of the Company's investment portfolio are liquidity and safety of principal. Investments are made with the objective of achieving the highest rate of return consistent with these two objectives. Our investment policy limits investments to certain types of debt and money market instruments issued by institutions primarily with investment grade credit ratings and places restrictions on maturities and concentration by type and issuer.

We review our available-for-sale securities for other-than-temporary declines in fair value below their cost basis on a quarterly basis and whenever events or changes in circumstances indicate that the cost basis of an asset may not be recoverable. This evaluation is based on a number of factors including, the length of time and extent to which the fair value has been less than our cost basis and adverse conditions specifically related to the security including any changes to the rating of the security by a rating agency.

## NOTE C - PROPERTY AND EQUIPMENT

The balance of property and equipment at October 31, 2013 and 2012 consisted of the following:

|   | Useful life<br>(years) | October 31, |              |
|---|------------------------|-------------|--------------|
|   |                        | 2013        | 2012         |
| Vehicles  | 5                      | \$ 292,662  | \$ 269,267   |
| Leasehold improvements                          | 5-8                    | 598,040     | 598,040      |
| Computers                                       | 3                      | 593,273     | 522,792      |
| Equipment                                       | 3-7                    | 1,223,096   | 1,126,415    |
| Furniture and fixtures                          | 10                     | 149,698     | 137,215      |
| Total   |                        | 2,856,769   | 2,653,729    |
| Less: Accumulated depreciation and amortization |                        | (1,880,346) | (1,540,358)  |
| Property and equipment, net                     |                        | \$ 976,423  | \$ 1,113,371 |

## NOTE D - INCOME TAXES

In June 2011, Pharma-Bio, Pharma-PR and Pharma-Serv obtained a Grant of Industrial Tax Exemption pursuant to the terms and conditions set forth in Act No. 73 of May 28, 2008 (“the Grant”) issued by the Puerto Rico Industrial Development Company (“PRIDCO”). The Grant was effective as of November 1, 2009 and covers a fifteen year period. The Grant provides relief on various Puerto Rico taxes, including income tax, with certain limitations, for most of the activities carried on within Puerto Rico, including those that are for services to parties located outside of Puerto Rico. The Grant establishes a threshold (“Baseline”) on the Industrial Development Income (“IDI”) subject to the favorable income tax rates. Within a four year term ending with the taxable year ending October 31, 2013, the Baselines were gradually reduced to zero. Certain activities covered under the Grant are not subject to a Baseline and are allowed a four year gradual phase-in from the maximum income tax rate of 30%, as provided by the 2011 Puerto Rico Internal Revenue Code, to the favorable fixed Act 73 income tax rate of 4%. In addition, IDI earnings distributions accumulated since November 1, 2009 are exempt from Puerto Rico earnings distribution tax.

Currently, Puerto Rico operations not covered under the exempt activities of the Grant are subject to Puerto Rico income tax at a maximum tax rate of 30%. Effective with our fiscal year end October 31, 2014, the maximum income tax rate under the Puerto Rico Internal Revenue Code will be 39%. The operations carried out in the United States by the Company’s subsidiary are taxed in the United States at a maximum regular federal income tax rate of 35%.

Distribution of earnings by the Puerto Rican subsidiaries to its parent 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. 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, federal and state taxes on operations in the United States, plus the earnings distribution tax in Puerto Rico from dividends paid to the Puerto Rican subsidiaries’ parent, and the parent’s federal income tax, if any, incurred upon the subsidiary’s earnings distribution.

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 reconciliation between the United States federal statutory rate and our effective tax rate for the years ended October 31, 2013, and 2012 is as follows:

|   | October 31, |         |
|---|-------------|---------|
|   | 2013        | 2012    |
| United States federal statutory rate  | 35.0%       | 35.0%   |
| Non United States earnings invested indefinitely, and Puerto Rico Act 73 Tax Grant effect | (15.7)%     | (17.0)% |
| Other, net  | -%          | 0.6%    |
| Effective tax rate  | 19.3%       | 18.6%   |

As of October 31, 2013 and 2012, the Company has not recognized deferred income taxes on \$14.4 million and \$10.5 million of undistributed earnings of its Puerto Rican subsidiaries, respectively, 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 Puerto Rico earnings distribution tax and United States federal income tax for the aggregate amount of approximately \$2.9 million and \$1.6 million at October 31, 2013 and 2012, respectively.

At October 31, 2013, Pharma-Spain and Pharma-IR have unused operating losses of approximately \$178,000 and \$727,000, respectively. These net operating losses are available to offset future taxable income until October 31, 2028 for Pharma-Spain and indefinitely for Pharma-IR. After considering various timing differences for income tax purposes, these unused operating losses result in a potential deferred tax asset for Pharma-Spain and Pharma-IR of approximately \$35,000 and \$90,000, respectively. 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. 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.

The Company files income tax returns in the United States (federal and various states jurisdictions), Puerto Rico, Ireland and Spain. Tax years ending October 31, 2008 through October 31, 2013 are open and may be subject to potential examination in one or more jurisdictions. During the fiscal year ended October 31, 2012, Pharma-Bio's federal income tax return for the year ended October 31, 2008 was examined by the United States Internal Revenue Service, no deficiencies were assessed. Currently, the Company has no federal, state, Puerto Rico or foreign income tax examination.

#### NOTE E – COMMITMENTS AND CONTINGENCIES

Capitalized lease obligations - The Company leases vehicles under non-cancelable capital lease agreements with a cost of \$200,158 (accumulated amortization of \$127,205 and \$87,174) as of October 31, 2013 and 2012, respectively. Amortization expense for vehicles under non-cancelable lease agreements amounted to \$40,032 and \$34,566 in the years ended October 31, 2013 and 2012, 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 October 31, 2013:

| Twelve months ending October 31, | Amount    |
|----------------------------------|-----------|
| 2014                             | \$ 36,402 |
| 2015                             | 24,293    |
| 2016                             | 24,242    |
| 2017                             | 6,264     |

|  |           |
|--|-----------|
| Total future minimum lease payments                | 91,201    |
| Less: Amount of imputed interest                   | ( 7,289)  |
| Present value of future minimum lease payments     | 83,912    |
| Current portion of obligation under capital leases | (32,188)  |
| Long-term portion                                  | \$ 51,724 |

Operating facilities - The Company conducts its administrative operations in office facilities which are leased under four different rental agreements.

F-13

---

In February 2012, the Company automatically renewed a lease agreement, with an affiliate of our principal executive officer, for the headquarters and laboratory testing facilities in Dorado, Puerto Rico. The renewal is for a term of five years with monthly rental payments of \$23,930, \$25,127, \$26,383, \$27,702 and \$29,087 for each of the five years under the lease. The 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.

In November 2011, the Company entered into a lease agreement for the U.S. office facilities located in Plymouth, Pennsylvania. The lease was for a five-year term with monthly rental payments of \$6,282 for the first three years and subsequent increases of four percent per year. During the 2013 fiscal year, the landlord filed for bankruptcy. The lease was renegotiated with a new landlord with an effective date of December 1, 2013. The new lease is for a term of seven years, with monthly rental payments of \$6,282 for the first three years, and \$6,596, \$6,794, \$6,998, and \$7,208, respectively, thereafter. The lease has a renewal option for a term of three years with monthly rental payments of \$7,424, \$7,647 and \$7,876, for each of the years, respectively.

The Company maintains office facilities in Cork, Ireland and Madrid, Spain. Both facilities are under month-to-month leases with monthly payments of approximately \$900 and \$1,900, respectively.

The Company leases certain apartments as dwellings for employees. The leases are under short-term lease agreements and usually are cancelable upon 30-day notification.

Minimum future rental payments under non-cancelable operating leases having remaining terms in excess of one year as of October 31, 2013 are as follows:

|                              | Amount       |
|------------------------------|--------------|
| 2014                         | \$ 388,212   |
| 2015                         | 403,854      |
| 2016                         | 420,277      |
| 2017                         | 166,101      |
| 2018                         | 81,330       |
| Thereafter                   | 177,261      |
| Total minimum lease payments | \$ 1,637,035 |

Rent expense during the years ended October 31, 2013 and 2012 was \$521,800 and \$411,100, respectively.

Contingencies - In the ordinary course of business, the Company may be a party to legal proceedings incidental to the business. These proceedings are not expected to have a material adverse effect on the Company's business or financial condition.



## NOTE F – WARRANTS

At October 31, 2013 and 2012, the Company had outstanding warrants to purchase shares of the Company's common stock as follows:

|                     | Exercise<br>Price | Expiration Date  | Outstanding Warrants<br>October 31, |           |
|---------------------|-------------------|------------------|-------------------------------------|-----------|
|                     |                   |                  | 2013                                | 2012      |
| Original Warrants A | \$ 0.06           | January 16, 2014 | 240,800                             | 240,800   |
| BrBroker Warrants B | \$ 0.06           | January 24, 2014 | -                                   | 1,830,991 |
| Warrants Total      |                   |                  | 240,800                             | 2,071,791 |

In January 2013, the holder of Broker Warrants B exercised its warrants to purchase 1,830,991 shares of common stock. All Original Warrants A were exercised by its holders in January 2014.

## NOTE G – CAPITAL TRANSACTIONS

On January 23, 2013, the Company entered into an agreement with an investor relations firm to assist in the Company's shareholder communication efforts. For these services, in addition to a monthly fee of \$10,000, the Company agreed to issue to the investor relations firm a total of 150,000 shares during the one year term of the agreement (75,000, 37,500 and 37,500 shares in January 2013, July 2013 and January 2014, respectively). As of January 24, 2014, pursuant to the terms of the agreement with the investor relations firm, all shares were issued.

## NOTE H – EARNINGS PER SHARE

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

|  | Years ended October 31, |              |
|--|-------------------------|--------------|
|  | 2013                    | 2012         |
| N Net t income available to common equity holders - used to compute basic and diluted earnings per share | \$ 4,906,489            | \$ 4,687,006 |
| WWeighted average number of common shares - used to compute basic earnings per share                     | 22,201,514              | 20,758,695   |
| Effect of warrants to purchase common stock  | 665,911                 | 1,919,849    |
| Effect of options to purchase common stock   | 792,937                 | 261,157      |
| WWeighted average number of shares - used to compute diluted earnings per share                          | 23,660,362              | 22,939,701   |

## 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, consultants and directors. 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. 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 the Company's 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.

The Company recognizes stock-based compensation 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 2005 Plan stock options activity and status for the years ended October 31, 2013 and 2012 was as follows:

|  | Year ended October 31, |                       | Year ended October 31, |                       |
|--|------------------------|-----------------------|------------------------|-----------------------|
|  | 2013                   |                       | 2012                   |                       |
|  | Number of              | Weighted-Average      | Number of              | Weighted-Average      |
|  | Shares                 | Option Exercise Price | Shares                 | Option Exercise Price |
| Outstanding at beginning of year                     | 1,740,000              | \$ 0.6965             | 454,585                | \$ 0.5804             |
| Granted  | 40,000                 | \$ 0.7500             | 1,355,000              | \$ 0.7372             |
| Exercised  | -                      |                       | -                      |                       |
| Expired and/or forfeited                             | (610,000)              | \$ 0.7257             | (69,585)               | \$ 0.7317             |
| Total outstanding at end of year                     | 1,170,000              | \$ 0.6831             | 1,740,000              | \$ 0.6965             |
| Outstanding exercisable stock options at end of year | 523,327                | \$ 0.6294             | 430,000                | \$ 0.5702             |

|  | October 31, 2013 | October 31, 2012 |
|--|------------------|------------------|
| Weighted average remaining years in contractual life for:                            |                  |                  |
| Total outstanding options  | 3.0 years        | 3.4 years        |
| Outstanding exercisable options  | 2.6 years        | 1.0 years        |
| Shares of common stock available for issuance pursuant to future stock option grants | 1,330,000        | 760,000          |

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

|                                     | Year ended October 31, |           |
|-------------------------------------|------------------------|-----------|
|                                     | 2013                   | 2012      |
| Stock-based compensation expense:   |                        |           |
| Cost of services                    | \$ 11,121              | \$ 10,000 |
| Selling, general and administrative | 42,040                 | 13,664    |

Edgar Filing: Pharma-Bio Serv, Inc. - Form 10-K

|                                      |            |            |
|--------------------------------------|------------|------------|
| Stock-based compensation before tax  | 53,161     | 23,664     |
| Income tax benefit                   | -          | -          |
| Net stock-based compensation expense | \$ 53,161  | \$ 23,664  |
| Effect on earnings per share:        |            |            |
| Basic earnings per share             | \$ (0.002) | \$ (0.001) |
| Diluted earnings per share           | \$ (0.002) | \$ (0.001) |

As of October 31, 2013, estimated stock based compensation expense to be recognized in future periods for granted nonvested stock options amounted to approximately \$60,000. These nonvested stock options compensation expense will be recognized in a weighted average period of approximately 0.8 years.

The fair value of stock-based awards to employees is calculated using the Black-Scholes option pricing model. The Black-Scholes model requires subjective assumptions, including future stock price volatility and expected time to exercise, which greatly affect the calculated values. The expected term of the option has been estimated using the “simplified” method as provided in (“SEC”) Staff Accounting Bulletin No. 107. Under this method, the expected term equals the arithmetic average of the vesting term and the contractual term of the option. The risk-free rate is based on the U.S. Treasury rates in effect during the corresponding period of grant. The expected volatility is based on the historical volatility of the Company’s stock price. These factors could change in the future, which would affect fair values of stock options granted in such future periods, and could cause volatility in the total amount of the stock-based compensation expense reported in future periods.

The following weighted average assumptions were used to estimate the fair value of stock options granted for the years ended October 31, 2013 and 2012:

|  | Year ended October 31, |           |
|--|------------------------|-----------|
|  | 2013                   | 2012      |
| Expected dividend yield                        | 0.0%                   | 0.0%      |
| Expected stock price volatility                | 47.7%                  | 40.9%     |
| Risk free interest rate                        | 0.4%                   | 0.3%      |
| Expected life of options                       | 3.2 years              | 3.5 years |
| Weighted average fair value of options granted | \$ 0.2495              | \$ 0.2227 |

As of October 31, 2013 and 2012, the aggregate intrinsic value of options outstanding was approximately \$1,108,000 and \$180,000, respectively. The aggregate intrinsic value represents the difference between the Company’s stock price at year end and the exercise price, multiplied by the number of in-the money options had all option holders exercised their options. This amount changes based on the fair market value of the Company’s stock. For the years ended October 31, 2013 and 2012, no stock options were exercised.

#### NOTE J - CONCENTRATION OF RISKS

##### Cash and cash equivalents

The Company domestic cash and cash equivalents consist of cash deposits in FDIC insured banks (substantially covered by FDIC insurance by the spread of deposits in multiple FDIC insured banks), a money market obligations trust registered under the US Investment Company Act of 1940, as amended, and U.S. Treasury securities with maturities of three months or less. In the foreign markets we serve, we also maintain cash deposits in foreign banks, which tend to be not significant and have no specific insurance. 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, Ireland and Spain. 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 three customers, who accounted for 10% or more of its revenues in either of the years ended October 31, 2013 or 2012. During the year ended October 31, 2013 revenues from these customers were 28%, 15% and 12%, or a total of 55%, as compared to the same period last year for 25%, 19% and 8%, or a total of 52%, respectively. At October 31, 2013 and 2012, amounts due from these customers represented 38% and 49% of total accounts receivable balance, respectively.

The major customer information in the above paragraph is based on revenues earned from said customers at the segment level because in management's opinion contracts by segments are totally independent of each other, and therefore such information is more meaningful to the reader. These revenues pertain to two global group of affiliated companies. During the year ended October 31, 2013, aggregate revenues from these global groups of affiliated companies were 51% and 12%, or a total of 63%, as compared to the same period last year for 54% and 8%, or a total of 62%, respectively. At October 31, 2013 and 2012, amounts due from this global group of affiliated companies represented 47% and 60% of total accounts receivable balance, respectively.

F-17

---

## NOTE K - SEGMENT DISCLOSURES

The Company's segments are based on the organizational structure for which financial results are regularly evaluated by the Company's chief operating decision maker to determine resource allocation and assess performance. Each reportable segment is managed by its own management team and reports to executive management. The Company has four reportable segments: (i) Puerto Rico technical compliance consulting, (ii) United States technical compliance consulting, (iii) Europe technical compliance consulting, and (iv) a Puerto Rico microbiological and chemical laboratory testing division ("Lab"). These reportable segments provide services primarily to the pharmaceutical, chemical, medical device and biotechnology industries in their respective markets.

The following table presents information about the reported revenue from services and earnings from operations of the Company for the year ended in October 31, 2013 and 2012. There is no intersegment revenue for the mentioned periods. Corporate expenses that support the operating units have been allocated to the segments. Asset information by reportable segment is not presented, since the Company does not produce such information internally, nor does it use such data to manage its business.

|  | Year ended October 31, |               |
|--|------------------------|---------------|
|  | 2013                   | 2012          |
| <b>REVENUES:</b>                           |                        |               |
| Puerto Rico consulting                     | \$ 15,833,248          | \$ 15,213,662 |
| United States consulting                   | 11,334,094             | 9,159,539     |
| Europe consulting                          | 3,596,648              | 3,211,758     |
| Lab (microbiological and chemical testing) | 1,866,935              | 857,948       |
| Other segments <sup>1</sup>                | 431,085                | 784,260       |
| Total consolidated revenues                | \$ 33,062,010          | \$ 29,227,167 |
| <b>INCOME (LOSS) BEFORE TAXES:</b>         |                        |               |
| Puerto Rico consulting                     | \$ 3,673,143           | \$ 3,664,238  |
| United States consulting                   | 2,227,771              | 2,407,190     |
| Europe consulting                          | (319,193)              | (245,431)     |
| Lab (microbiological and chemical testing) | 250,500                | (381,406)     |
| Other segments <sup>1</sup>                | 244,089                | 311,021       |
| Total consolidated income before taxes     | \$ 6,076,310           | \$ 5,755,612  |

<sup>1</sup> Other segments represent activities that fall below the reportable threshold and are carried out in Puerto and United States. These activities include a technical seminars/training division, an information technology services and consulting division, and corporate headquarters, as applicable.

Long lived assets (property and equipment) and related depreciation and amortization expense for the year ended October 31, 2013 and 2012, were concentrated in the domestic markets (Puerto Rico and United States). The aggregate amount of long lived assets for the international operations (Europe) is considered insignificant.



NOTE L - RETIREMENT PLAN

Pharma-PR has a qualified profit sharing plan in accordance with the provision of Section 1081.01 of the Puerto Rico Code, for employees who meet certain age and service period requirements. The Company makes contributions to this plan as required by the provisions of the plan document. Contributions for the years ended October 31, 2013 and 2012 were \$91,500 and \$75,100, respectively.

NOTE M – RELATED PARTY TRANSACTIONS

Our Chairman of the Board of Directors, stepped down as President and Chief Executive Officer of the Company, effective December 31, 2012. On January 7, 2013, the Company entered into a Consulting Agreement with our Chairman, effective as of January 1, 2013 (the "Consulting Agreement"). Pursuant to the Consulting Agreement, the Chairman will serve as the Company's Senior Strategic Consultant to provide advice and assistance to the Board of Directors and the officers of the Company. Pursuant to the Consulting Agreement, the Chairman will receive a consulting fee on a per hour basis, subject to an aggregate amount not to exceed \$300,000 during the one year term of the Consulting Agreement. Additionally, the Chairman will receive a company automobile and such insurance as she was provided by the Company during her last year of employment with the Company. The Consulting Agreement also includes standard provisions relating to non-competition, confidentiality, and non-disparagement. On July 17, 2013, the Compensation Committee of the Board of Directors of the Company approved up to 720 additional hours of consulting services to be provided by the Chairman at the previously established rate of \$275 per hour during the one year term of the Consulting Agreement.

On December 31, 2013, the Company entered into a Consulting Agreement with a company (the "Consultant") affiliated to our Chairman and our Chairman, effective as of January 1, 2014. Pursuant to the Consulting Agreement, the Consultant will consult with the Board regarding the Company's strategic initiatives, company services, management, operations and other matters as may be requested from time to time by the Board. Pursuant to the Consulting Agreement, the Consultant will receive a monthly fee of \$42,000 during the one year term of the Consulting Agreement. Additionally, our Chairman will receive a company automobile and such insurance as she was provided by the Company during her last year of employment with the Company. The Consulting Agreement also included standard provisions relating to non-competition, confidentiality, non-transferability and non-disparagement.