INFINITE GROUP INC
Form 10QSB
July 26, 2005

UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-QSB

QUARTERLY REPORT UNDER SECTION 13 OR 15(D)
OF THE SECURITIES EXCHANGE ACT OF 1934
FOR THE QUARTERLY PERIOD ENDED MARCH 31, 2004

Commission File Number 0-21816

INFINITE GROUP INC.
(Exact name of small business issuer as specified in its charter)

Delaware	52-1490422
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

595 Blossom Rd. Suite 309
Rochester, New York 14610
(Address of principal executive office)

(585) 654-5525
(Issuer's telephone number, including area code)

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

Yes |_| No |X|

Number of shares outstanding of each of the issuer's classes of common equity, as of the latest practicable date: As of July 15, 2005, there were 19,206,965 shares of common stock outstanding.

Transitional Small Business Disclosure Format. Yes |_| No |X|

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FORM 10-QSB REPORT

Infinite Group Inc.

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FORWARD-LOOKING STATEMENTS

Certain statements made in this Quarterly Report on Form 10-QSB are "forward-looking statements" within the meaning of Section 21E of the Securities and Exchange Act of 1934 regarding the plans and objectives of management for future operations and market trends and expectations. Such statements involve 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 such forward-looking statements. The forward-looking statements included herein are based on current expectations that involve numerous risks and uncertainties. Our plans and objectives are based, in part, on assumptions involving the continued expansion of our business. Assumptions relating to the foregoing involve judgments with respect to, among other things, future economic, competitive and market conditions and future business decisions, all of which are difficult or impossible to predict accurately and many of which are beyond our control. Although we believe that our assumptions underlying the forward-looking statements are reasonable, any of the assumptions could prove inaccurate and, therefore, there can be no assurance that the forward-looking statements included in this report will prove to be accurate. In light of the significant uncertainties inherent in the forward-looking statements included herein, the inclusion of such information should not be regarded as a representation by us or any other person that our objectives and plans will be achieved. The terms "we", "our", "us", or any derivative thereof, as used herein refer to Infinite Group Inc., a Delaware corporation.

PART I
FINANCIAL INFORMATION

Item 1. Financial Statements

INFINITE GROUP, INC.

Consolidated Balance Sheets

	March 31, 2004	December 3 2003
ASSETS	(Unaudited)	
Current assets:		
	$ 30,706	$ 16,5
Restricted cash	52,733	26,5
Accounts receivable, net of allowance	554,198	165,8
Other current assets	9,108	1,0
Assets held for sale	2,853,758	2,919,1
Assets of discontinued operations	866,893	870,2
Total current assets	4,367,396	3,999,3
Property and equipment, net	98,190	99,4
Other assets:		
Note receivable	73,897	73,8
Intangible assets, net	59,735	62,9
Total other assets	133,632	136,8
Total assets	$ 4,599,218	$ 4,235,5
LIABILITIES AND STOCKHOLDERS' DEFICIENCY		
Current liabilities:		
Notes payable:		
Bank	158,910	152,1
Other	30,000	30,0
Related parties	9,906	9,9
Accounts payable	678,914	613,7
Accrued expenses	444,830	359,8
Current maturities of long-term obligations	2,293,116	2,360,8
Liabilities held for sale	862,460	781,8
Liabilities of discontinued operations	963,248	933,3
Total current liabilities	5,441,384	5,241,5
Long-term obligations		
Bank notes payable	24,543	32,8
Notes payable-related parties	1,158,124	887,1
Accrued pension expense	2,186,982	2,190,2
Total liabilities	8,811,033	8,351,7
Commitments and contingencies		
Stockholders' deficiency:		
Common stock, $.001 par value, 20,000,000 shares authorized; 14,244,465 (10,624,465-2003) shares issued and outstanding	14,244	10,6
Additional paid-in capital	28,203,890	28,026,5
Common stock, 1,500,000 authorized, not issued	--	75,0
Accumulated deficit	(29,543,203)	(29,297,9
Accumulated other comprehensive loss	(2,886,746)	(2,930,3

Total stockholders' deficiency	(4,211,815)	(4,116,1
Total liabilities and stockholders' deficiency	$ 4,599,218	$ 4,235,5

See notes to consolidated financial statements.

INFINITE GROUP, INC.

Consolidated Statements of Operations (Unaudited)

	Three Months Ended March 31,	
	2004	2003
		(As Restated)
Sales	$ 560,435	$ 1,203
Cost of goods and services	359,986	--
Gross profit	200,449	1,203
Costs and expenses:		
General and administrative	264,180	181,487
Depreciation and amortization	6,606	--
Selling	169	--
Research and development	68,646	1,932
Total costs and expenses	339,601	183,419
Operating loss	(139,152)	(182,216)
Other income (expense):		
Interest expense-related parties	(17,088)	(1,356)
Total other income (expense)	(17,088)	(1,356)
Loss from continuing operations before income tax expense	(156,240)	(183,572)
Income tax expense	(350)	--
Loss from continuing operations	(156,590)	(183,572)
Loss from discontinued operations	(88,669)	(227,551)
Net loss	$ (245,259)	$ (411,123)
Net loss per share basic and diluted:		
Loss from continuing operations	$ (.01)	$ (.03)
Income (loss) from discontinued operations	(.01)	(.03)
Net loss	$ (.02)	$ (.06)

Weighted average number of shares outstanding: Basic and Diluted	12,987,762	6,314,077

See notes to consolidated financial statement.

INFINITE GROUP, INC.

Consolidated Statements of Cash Flows (Unaudited)

	Three M Ma
	2004
Operating activities:	
Net loss	$ (245,259)
Adjustments to reconcile net loss to net cash provided by (used in) operating activities:	
Loss from discontinued operations	88,669
Depreciation and amortization	6,606
(Increase) decrease in:	
Accounts receivable, net	(388,368)
Other current assets	(8,048)
Increase (decrease) in:	
Accounts payable and accrued expenses	150,228
Accrued pension obligations	40,386
Net cash provide by (used in) operating activities of continuing operations	(355,786)
Net cash provided by (used in) operating activities of discontinued operations	92,223
Net cash provided (used in) by operating activities	(263,563)
Investing activities:	
Increase in restricted funds for asset addition, net	(26,233)
Purchase of property and equipment	(3,768)
Net cash provided by (used in) investing activities of continuing operations	(30,001)
Net cash provided by (used in) investing activities discontinued operations	--
Net cash provided by (used in) investing activities	(30,001)
Financing activities:	
Net (repayments) borrowings of bank notes payable	6,788
Proceeds from issuance of long-term obligations-related parties	342,000
Repayment of notes payable-related parties	(71,000)
Repayment of long-term obligations	(76,033)
Proceeds from issuance of common stock, net of costs	106,000
Net cash provided by (used in) financing activities	307,755
Net increase (decrease) in cash	14,191
Cash - beginning of period	16,515

Cash - end of period	$ 30,706
Supplemental disclosure:	
Cash paid for:	
Interest	$ (536)
Income taxes	$ (350)

See notes to consolidated financial statements.

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INFINITE GROUP INC.

Notes to Consolidated Financial Statements-(Unaudited)

Note 1. Basis of Presentation

The accompanying unaudited consolidated financial statements of Infinite Group Inc. ("Infinite Group Inc." or the "Company"), included herein have been prepared by the Company in accordance with accounting principles generally accepted in the United States of America for interim financial information and with instructions to Form 10-QSB. Accordingly, they do not include all of the information and footnotes required by accounting principles generally accepted in the United States of America for complete financial statements. In the opinion of management, all adjustments considered necessary for a fair presentation have been included. All such adjustments are of a normal recurring nature. The accompanying unaudited consolidated financial statements should be read in conjunction with the Company's audited consolidated financial statements and footnotes for the year ended December 31, 2003 and the notes thereto included in the Company's Annual Report on Form 10-KSB filed with the United States Securities and Exchange Commission. Results of consolidated operations for the three month period ended March 31, 2004 are not necessarily indicative of the operating results that may be expected for the year ended December 31, 2004. The consolidated financial statements herein include the accounts of the Company and its wholly owned subsidiaries. All material inter-company accounts and transactions have been eliminated.

Note 2. Summary of Significant Accounting Policies

Critical Accounting Policies and Estimates

There are several accounting policies that we believe are significant to the presentation of our consolidated financial statements. These policies require management to make complex or subjective judgments about matters that are inherently uncertain. Note 3 to our audited consolidated financial statements present a summary of significant accounting policies. The most critical accounting policies follow.

Revenue Recognition

Beginning in the second quarter of 2003, we commenced providing services in the field of information technology (IT) consulting services through our IT Services Group. Consulting revenues are recognized as the consulting services are provided. Customer deposits received in advance are recorded as liabilities until associated services are completed.

Stock-Based Compensation

We disclose the pro forma compensation cost relating to stock options granted under employee stock option plans, based on the fair value of those options at the date of grant. This valuation is determined utilizing the Black-Scholes, option-pricing model, which takes into account certain assumptions, including the expected life of the option and the expected stock volatility and dividend yield over this life. These assumptions are made based on past experience and expected future results. In the event the actual performance varies from the estimated amounts, the value of these options may be misstated.

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Effect of New Accounting Pronouncements

In June 2001, the FASB issued Statement of Financial Accounting Standards (SFAS) No. 141, "Business Combinations," and SFAS No. 142, "Goodwill and Other Intangible Assets." Under these new standards, all acquisitions subsequent to June 30, 2001 must be accounted for under the purchase method of accounting.

SFAS No. 142 requires that goodwill be tested annually for impairment using a two-step process. The first step was to identify a potential impairment and, in transition, this step must be measured as of the beginning of the fiscal year. The second step of the goodwill impairment test measures the amount of the impairment loss (measured as of the beginning of the year of the adoption), if any, and must be completed by the end of our fiscal year. Any impairment loss resulting from the transitional impairment tests are reflected as the cumulative effect of a change in accounting principle.

We adopted the provisions of SFAS No. 142 in our first quarter ended March 31, 2002. Goodwill in the amount of $88,769 at December 31, 2001, relates to the Laser Fare (LF) and Mound subsidiaries. Subsequent to December 31, 2001, the assets of Mound were disposed of and operations were ceased, resulting in the write-down of goodwill amounting to $17,584. In addition the goodwill relating to Laser Fare, amounting to $71,185 was written off at December 31, 2002. We have allocated its intangible assets to its reporting units. The remaining useful lives of the intangibles have been evaluated and no changes will be made.

SFAS No. 141 also requires that upon adoption of SFAS No. 142, the Company reclassify the carrying amounts of certain intangibles assets into or out of goodwill, based upon certain criteria. We do not anticipate any reclassifications. SFAS No. 142 supersedes APB No. 17, "Intangible Assets," and is effective for fiscal years beginning after December 15, 2001. SFAS No. 142 primarily addresses the accounting for goodwill and intangible assets subsequent to their initial recognition. The provisions of SFAS No. 142 prohibit the amortization of goodwill and indefinite-lived intangible assets; require that goodwill and indefinite-lived intangible assets be tested annually for impairment, and in interim periods if certain events occur indicating that the carrying value of goodwill and / or indefinite-lived intangible assets may be impaired; require that reporting units be identified for the purpose of assessing potential future impairments of goodwill; and removes the 40-year limitation on the amortization period of intangible assets that have finite lives.

In August 2001, the FASB issued SFAS No. 143, "Accounting for Asset Retirement Obligations" (SFAS 143). SFAS 143 establishes accounting standards for recognition and measurement of a liability for the costs of asset retirement obligations. Under SFAS 143, the costs of retiring an asset will be recorded as a liability when the retirement obligation arises, and will be amortized to expense over the life of the related asset.

In August 2001, the Financial Accounting Standards Board issued Statement No.

144 (SFAS 144), "Accounting for the Impairment or Disposal of Long-Lived Assets", which provides guidance in the accounting for impairment of disposal of long-lived assets. For long-lived asset to be held and used, the new rules are similar to previous guidance, which required the recognition of impairment when the undiscounted cash flows will not recover the carrying amount. The computation of fair value now removes goodwill from consideration and incorporates a probability-weighted cash flow estimation approach. Additionally, assets qualifying for discontinued operations treatment have been expanded beyond the former major line of business or class of customer approach. We adopted the provisions of SFAS 144 in fiscal 2001 and utilized this guidance for the disposal of the Plastics Group. Accordingly, the assets and liabilities of the discontinued operations are reflected as gross amounts, rather than net, in the accompanying balance sheet in accordance with SFAS 144. There was no impact from the adoption of this standard on its impairment tests of long-lived assets or its accounting for discontinued operations.

In April 2002, the FASB issued SFAS 145 "Rescission of SFAS No. 4, 44 and 64, "Amendment of SFAS No.13, and Technical Corrections". SFAS No. 145, among other things, amends SFAS No. 4 and SFAS No. 64, to require that gains and losses from the extinguishments of debt generally be classified within continuing operations. The provisions of SFAS No. 145 are effective for fiscal years beginning after May 15, 2002 and early application is encouraged. We do not believe that the adoption of SFAS No. 145 will have a significant impact on our financial statements.

In June 2002, the FASB issued SFAS 146, "Accounting for Costs Associated with Exit or Disposal Activities." SFAS 146 replaces Emerging Issues Task Force ("EITF") Issue 94-3, "Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity". This standard requires companies to recognize costs associated with exit or disposal activities when they are incurred rather than at the date of a commitment to an exit or disposal plan. This statement is effective for exit or disposal activities that are initiated after December 31, 2002. We do not believe that the adoption of SFAS No. 146 will have a significant impact on our financial statements.

In February 2003, the FASB issued SFAS No. 148, "Accounting for Stock Based Compensation: A Comparison of FASB Statement No. 123, Accounting for Stock-Based Compensation, and Its Related Interpretations, and IASB Proposed IFRS, Share-based Payments." SFAS 148 amends SFAS 123 to provide alternative methods of transition for an entity that voluntarily changes to the fair value based method of accounting for stock-based employee compensation. It also amends the disclosure provisions of that Statement to require prominent disclosure about the effects on reported net income of an entity's accounting policy decisions with respect to stock-based compensation. The statement also amends APB Opinion No. 28, "Interim Financial Reporting", to require disclosure about those effects in interim financial information. We have chosen not to voluntarily change to the fair value based method of accounting for stock-based employee compensation but have adopted the disclosure rules under SFAS 148.

Note 3. Discontinued Operations and Reclassifications

The statements of operations and cash flows for the three months ended March 31, 2003 have been restated to account for the discontinued operations of the Laser Group, which was sold as discussed below.

On October 30, 2002, IPI received a Notice of Termination of its DARPA contract for the government's convenience under the contract provisions entitled Termination, Federal Acquisition Regulation (FAR) 52.249.6. The DARPA contract had provided substantially all of the revenue of the Photonics Group. As of

December 31, 2004, the contract termination process was substantially complete. We have been reimbursed for substantially all costs associated with the termination. The termination of the contract had a detrimental effect on the development of our technology. During 2002, all of our Photonics Group employees were released and the operations of the Photonics Group ceased. We also determined that our Photonics Group patents and property and equipment were impaired, and consequently recorded impairment losses in the fourth quarter of 2002 of approximately $468,000 and $148,000 respectively, which was included in loss on disposal of discontinued operations in the consolidated statement of operations for the year ended December 31, 2002.

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On December 31, 2003, the Company and LF entered into an asset purchase agreement with LFI, Inc. ("LFI") relating to the purchase by LFI of certain assets and the assumption of certain liabilities of LF relating to the laser engraving and medical products manufacturing and assembly businesses of LF (the "Purchase Agreement"). The principals of LFI are former employees of LF, including the former chairman and chief executive officer of the Company. The purchase price for the assets was assumed liabilities of LF and/or the Company. On December 31, 2004, the Company completed the sale of the remaining assets, including the assumption of certain liabilities, to an affiliate of LFI, relating to all the remaining laser businesses of LF. The purchase price was the assumed liabilities of LF plus the issuance of several notes by the buyer to LF. LF recorded a loss on sale of approximately $99,000 for the year ended December 31, 2003. LF reclassified the operating assets and liabilities to assets and liabilities held for sale at December 31, 2003. The balances of the assets held for sale at December 31, 2003 was $2,919,154 with related liabilities of $781,847. During the year ended December 31, 2003, LF had loss from operations of approximately $417,000.

In accordance with FASB 144, the disposal of the Photonics and Laser segments have been accounted for as a disposal of business segments and accordingly, the assets and liabilities for IP and LF have been segregated from continuing operations in the accompanying consolidated balance sheets and classified as assets of discontinued operations and assets held for sale. The operating results for both segments are segregated and reported as discontinued operations in the accompanying consolidated statements of operations and cash flows.

The following is a summary of financial position at March 31, 2004 and December 31, 2003 and results of operations for the three months ended at March 31, 2003 and March 31, 2004 for the disposed Photonics (IP), Plastics (O&W and EP) and Laser Fare (LF).

Financial Position	March 31, 2004	December 31, 2003
Assets held for sale:		
Current assets	$ 879,946	$ 858,949
Property and equipment	1,973,812	2,060,205
Total assets held for sale	$ 2,853,758	$ 2,919,154
Accounts payable and accrued expenses held for sale	$ 862,460	$ 781,847

Current assets and total assets of discontinued operations	$ 866,893	$ 870,287
Liabilities of discontinued operations:		
Accounts payable and accrued expenses	$ 958,248	$ 928,349
Unsecured note payable	5,000	5,000
Total liabilities of discontinued operations	$ 963,248	$ 933,349

Results of Operations	Three Months Ended March 31, 2004	2003
Revenue from discontinued operations	$ 670,510	$ 1,545,472
Loss from discontinued operations	$ (88,669)	$ (227,551)
Loss on disposal of discontinued operations	--	--
Net loss from discontinued operations	$ (88,669)	$ (227,551)

Certain other amounts in the 2003 financial statements have been reclassified to conform with the 2004 financial statement presentations.

Note 4. Stock Option Plans

As of March 31, 2004 the Company's Stock Option Plans (the "Plan") provided for the grant of incentive or non-qualified stock options for the purchase of common stock for up to 2,340,000 shares to employees, directors and consultants. The Plan is administered by the compensation committee established by the Company's board of directors, which determines the terms of options including the exercise price, expiration date, number of shares and vesting provisions.

A summary of all stock option activity for the three months ended March 31, 2004 is as follows:

	Number Of Options	Exercise Price	Weighted Average Exercise Price
Outstanding at December 31, 2003	1,687,575	$ .05-2.50	$ .16

Options issued	68,500	$ .01-.07	$ .04
Options expired	(21,129)	$ 1.50-$2.50	$ 1.30
Outstanding at March 31, 2004	1,734,946	$ .01-$ 2.50	$ .14
Exercisable at March 31, 2004	1,668,279	$ .01-$2.50	$ .14

The Company has adopted the disclosure-only provisions of Statement of Financial Accounting Standards (SFAS) No. 123 -"Accounting for Stock-Based Compensation, " and, accordingly, does not recognize compensation cost for stock option grants under fixed awards. If the Company had elected to recognize compensation costs based on the fair value of the options granted at grant date as prescribed by SFAS No.123, net loss and loss per share from continuing operations would have increased as follows:

	Three Months Ended March 31,	
Results of Operations	2004	2003
Net loss-as reported (000's)	$ (245)	$ (411)
Total stock based employee compensation expense determined employee compensation expense determined under the fair value method for all awards (000's)	$ 7	$ 7
Net Loss- pro forma (000's)	$ (252)	$ (418)
Loss per share as reported	$ (.02)	$ (.06)
Loss per share pro forma	$ (.02)	$ (.06)

Note 5. Business Segments

Prior to 2002, the Company's business were organized, managed and internally reported as three segments. The segments are determined based on differences in products, production processes and internal reporting. During the year ended December 31, 2001, the Company approved of a plan to discontinue the operations of the Plastics Group. During the fourth quarter of 2002, the Company's contract with DARPA was terminated and as a result of the termination, management decided to suspend the activities of the Photonics Group in 2002 and liquidate the remaining assets. During the fourth quarter of the year ended December 31, 2003, the Company approved the sale of the assets and certain liabilities of its Laser Fare, Inc. subsidiary, referred to as the Laser Group. As a result, in accordance with FASB 144, the disposal of the Plastics, Photonics, and Laser segments have been accounted for as disposals of business segments and accordingly, the respective assets (liabilities) have been segregated from continuing operations and classified as assets of discontinued operations and the operating results for all three segments are segregated and reported as

discontinued operations.

Beginning in 2003, the Company revised its business strategy and began operating its newly formed IT Services Group.

All of the segments of the Company operate entirely within the United States. Revenues from customers in foreign countries are minimal. The Company relies on inter-segment cooperation and management does not represent that these segments, if operated independently, would report the results shown.

A summary of selected consolidated information for the Company's industry segments during the periods ended March 31, 2004 and 2003, respectively, is set forth as follows.

	Photonics Group	Laser Group	IT Services Group	Consol
Three Months ended March 31, 2003				
Sales to unaffiliated customers	$ --	$ --	$ 1,203	$
Operating loss	$ --	$ --	$ (182,216)	$ (1
Income (loss) from discontinued operations	$ (71,625)	$ (155,926)	$ --	$ (2
Three Months ended March 31, 2004				
Sales to unaffiliated customers	--	$ --	$ 560,435	$ 5
Operating loss	--	$ --	$ (139,152)	$ (1
(Loss) from discontinued operations	$ (40,179)	$ (48,490)	$ --	$ (

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Note 6. Non-Cash Transactions

Non-cash investing and financing transactions, including non-monetary exchanges, consist of the following:

	Three Months Ended March 31, 2004	2003
Common stock authorized not issued, transferred to issued	$ 75,000	$ --

Note 7. Earnings Per Share

Basic income per share is based on the weighted average number of common shares outstanding during the periods presented. Diluted income per share is based on the weighted average number of common shares outstanding, as well as dilutive potential common shares which, in the Company's case, comprise shares issuable under the stock options and stock warrants. The treasury stock method is used to calculate dilutive shares, which reduces the gross number of dilutive shares by the number of shares purchasable from the proceeds of the options assumed to be exercise. In a loss year, the calculation for basic and diluted earnings per share is considered to be the same, as the impact of potential common shares is anti-dilutive.

As of March 31, 2003 and 2004, all outstanding stock options and warrants have not been considered common stock equivalents because their assumed exercise would be anti-dilutive.

Item 2. Management's Discussion and Analysis of Financial Conditions and Results of Operations

On January 3, 2003, our former president and chief executive officer, Clifford G. Brockmyre II, resigned and was replaced by Michael S. Smith, one of our board members. At the same time, we moved our corporate headquarters from Rhode Island to Rochester, New York. On May 6, 2003, Dr. Allan Robbins and Paul Delmore were appointed to fill two existing vacancies on our board. Mr. Brockmyre remained on our board of directors until October 30, 2003 at which time he resigned. On March 15, 2004, Brian Corridan resigned from our board.

In the fourth quarter of 2003, we decided to dispose of our Laser Fare, Inc. subsidiary (LF) and to restructure our business. We sold a portion of the business of LF (primarily the medical and engraving business) as of December 31, 2003 and the remaining business as of December 31, 2004, although we continued to operate the business during the disposal process.

The purchase price for the assets consisted of LFI's assumption of certain of our liabilities in the aggregate amount of approximately $358,000. On December 31, 2004, we sold the remaining assets of LF to Rolben Acquisition Corporation (Rolben), a company affiliated with LFI. The purchase price for the remaining assets consisted of Rolben's assumption of substantially all of the liabilities of LF and the delivery of promissory notes in the aggregate amount of approximately $2.1 million. Because certain required consents were not yet obtained at December 31, 2004, we remained obligated under several notes to UPS Capital Business Credit (UPS) and the Rhode Island Industrial Facilities Corporation (RIIFC) in the same amounts as the notes from Rolben. These notes were refinanced by the acquirer in June 2005 and we are therefore no longer obligated under the several notes.

During the second quarter of 2003, we commenced providing services in the field of information technology (IT) consulting services through our IT Services Group. We provide business and technology integration and systems support to government clients. We focus on aligning business processes with technology for delivery of solutions meeting the client's exact needs.

Results of operations

Comparison of Three Months ended March 31, 2004 and 2003

We commenced the operations of our IT Services Group in the second quarter

of 2003. The following results include the operations of our IT Services Group beginning in 2003. The trends suggested by this table are not necessarily indicative of future operating results due to the start up nature of our IT Services Group.

	Three Months Ended March 31,			
	2004	As a % of Net Revenues	2003 (As Restated)	As a % o Revenu
Sales	$ 560,435	100.0 %	$ 1,203	100.0%
Cost of sales	359,986	64.2	--	0.0
Gross profit	200,449	35.8	1,203	100.0
General and administrative	264,180	47.1	181,487	15,086.2
Depreciation and amortization	6,606	1.2	--	0.0
Selling	169	0.0	--	0.0
Research and development	68,646	12.2	1,932	160.6
Total operating expenses	339,601	60.6	183,419	15,246.8
Operating loss	(139,152)	(24.8)	(182,216)	(15,146.8)
Other income (expense) and income taxes, net	(17,438)	(3.1)	(1,356)	(112.7)
Loss from continuing operations	(156,590)	(27.9)	(183,572)	(15,259.5)
Income (loss) from discontinued operations	(88,669)	(15.8)	(227,551)	(18,915.3)
Net loss	$(245,259)	(43.8)%	$(411,123)	(34,174.8)

Sales

Sales for the three months ended March 31, 2004 increased substantially by $559,232 to $560,435 as compared to net sales for the three months ended March 31, 2003 of $1,203. The increase was due to the start up of our IT Services Group, which began operations in the second quarter of 2003. We realized sales increases from new contracts with prime contractors for the U.S. Government. During 2003, we began to operate our new IT Services Group and its business base was still developing.

Cost of Sales and Gross Profit

Cost of sales represents the cost of employee services related to the IT Services Group. Cost of sales for the three months ended March 31, 2004 was $359,986 or 64.2% of sales as compared to no cost of sales for the three months ended March 31, 2003. Gross profit was $200,449 or 35.8% of sales for the three months ended March 31, 2004 compared to $1,203 or 100% of sales for the three months ended March 31, 2003. Gross profit as a percent of sales in 2004 is based on a relatively low volume of sales and is not necessarily indicative of gross margins that we will earn as our sales grows. We expect that gross margin as a percent of sales may decrease as sales increases due to the competitive nature of our business.

General and Administrative Expenses

General and administrative expenses include corporate overhead such as compensation and benefits for administrative and finance personnel, rent, insurance, professional fees, travel, and office expenses. General and administrative expenses for the three months ended March 31, 2004 increased by $82,693 or 45.6% due to the increases in employee compensation and related fringe benefits expenses as well as increased operating expenses as we manage a larger volume of business. General and administrative expense for the three months ended March 31, 2004 was $264,180 or 47.1% of sales which represented an increase from $181,487 in 2003, which was increased during the startup of sales from our IT Services Group. We anticipate that general and administrative expenses will increase as we continue to transition our business strategy and incur travel and other expenses associated with managing a larger business. We expect increases in accounting and legal expenses in 2004 and 2005 due to our focus on completing audits of our financial statements and related public information filings.

General and administrative expense includes expenses of the Osley & Whitney defined benefit retirement plan of approximately $40,000 and $50,000 for the three months ended March 31, 2004 and 2003, respectively.

Depreciation and Amortization

Depreciation and amortization expense was $6,606 for the three months ended March 31, 2004 compared to none for the three months ended March 31, 2003. This was due to establishing our new corporate headquarters in Rochester, New York in 2003 and the write off or disposition of assets in our former headquarters in Rhode Island. We began acquiring depreciable assets in the second quarter of 2003.

Selling Expenses

For the three months ended March 31, 2004 we incurred selling expenses of $169 associated with growing business in our IT Services Group. We expect selling expenses to increase as we generate sales opportunities and grow our IT Services Group.

Research and Development

For the three months ended March 31, 2004 we continued to incur research and development expenses associated with growing business in our IT Services Group related to our biometrics applications and recorded $68,646 of expense compared to $1,932 for the three months ended March 31, 2003. These expenses are principally related to the development of an access control terminal and related software called TouchThru(TM). TouchThru(TM) is a self-contained terminal enabling physical access control using biometric identification. It incorporates fingerprint matching technology licensed from Ultra-Scan Corporation, a private technology company headquartered in Buffalo, New York. TouchThru(TM) will be the first biometric product we introduce, and we intend to be in a position to market and sell that product beginning in 2006. We plan to market and sell TouchThru(TM) in a variety of industries and markets, including the federal, state and local government, health care, travel and general security, and access control.

Income (Loss) From Operations

For the three months ended March 31, 2004 our operating loss was $139,152 loss compared to a loss from operations of $182,216 in the comparable period of 2003. This is primarily attributable to our focus on our new IT Services Group and the

growth of IT sales which provided gross profit of $200,449 to fund research and development, general and administrative expense and interest expenses.

Other Income (Expense)

Other income and expense consists of interest expense on indebtedness for the three months ended March 31, 2004. Interest expense was $17,438 for the three months ended March 31, 2004 compared to $1,356 for the three months ended March 31, 2003, which was an increase of $16,082 for the periods due to an increase in borrowings from related parties.

Loss from Discontinued Operations

We recorded a loss from discontinued operations of $88,669 for the three months ended March 31, 2004 compared to a loss of $227,551 for the three months ended March 31, 2003. The loss is the result of the Photonics Group which was reclassified as discontinued operations and a loss from discontinued operations was recorded.

Net Income (Loss)

For the three months ended March 31, 2004, we recorded a loss from continuing operations of $156,590 or $(.01) per share and net loss of $245,259, or $(.02) per share. This compares to a net loss from continuing operations of $183,572 or $(.03) per share and a net loss of $411,123 or $(.06) per share (the difference of $(.03) per share is from discontinued operations) for the three months ended March 31, 2003. The reduction in loss is attributable to growth of sales and gross profit from our new IT Services which allowed us to fund our research and development, general and administrative, and interest expenses.

Liquidity and Capital Resources

As of March 31, 2004 we had unrestricted cash of approximately $31,000, which is available for working capital and property and equipment acquisition.

At March 31, 2004 we had a working capital deficit of approximately $1,074,000 (approximately $2,969,000 after eliminating the assets and liabilities of our discontinued operations and assets and liabilities held for sale). Approximately $2,300,000 of this deficit is caused by bank loan covenant violations resulting in the classification of long term maturities as current liabilities.

We have financed the activity of our new IT Services Group through the issuance of notes payable to related parties and private placements of common stock. In the future, we may issue additional debt or equity securities to satisfy our cash needs. Any debt incurred or issued may be secured or unsecured, at a fixed or variable interest rates and may contain other terms and conditions that our board of directors deems prudent. Any sales of equity securities may be at or below current market prices. We cannot assure you that we will be successful in generating sufficient capital to adequately fund our liquidity needs.

Risk Factors

You should consider the risk factors included in our Annual Report on Form 10-KSB in evaluating our business and us. Additional risks and uncertainties not presently known to us, which we currently deem immaterial or that are similar to those faced by other companies in our industry or business in general, such as competitive conditions, may also impair our business operations. If any of the results of the risks occur, our business, financial condition, or results of operations could be materially adversely affected.

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Item 3. Controls and Procedures

Evaluation of Disclosure Controls and Procedures. Our management, with the participation of the chief executive officer and the chief financial officer, carried out an evaluation of the effectiveness of our "disclosure controls and procedures" (as defined in the Securities Exchange Act of 1934 (the "Exchange Act") Rules 13a-15(e) and 15-d-15(e)) as of the end of the period covered by this report (the "Evaluation Date"). Based upon that evaluation, the chief executive officer and the chief financial officer concluded that, as of the Evaluation Date, our disclosure controls and procedures are effective, providing them with material information relating to the company as required to be disclosed in the reports we file or submit under the Exchange Act on a timely basis.

Changes in Internal Control over Financial Reporting. There were no changes in our internal controls over financial reporting, known to the chief executive officer or the chief financial officer, that occurred during our fiscal first quarter that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

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PART II

OTHER INFORMATION

Item 1: Legal Proceedings.

We are the plaintiff in a lawsuit filed in the Superior Court, State of Rhode Island on August 13, 1999 captioned Infinite Group, Inc. vs. Spectra Science Corporation and Nabil Lawandy. In the action, we assert that by fraud and in breach of fiduciary duties owed, Spectra and its president, Nabil Lawandy, caused us to sell to Spectra shares of Spectra's Series A Preferred stock at a substantial discount to fair market value. We allege that in entering into the transaction we relied on various representations made by Spectra and Mr. Lawandy, which were untrue at the time they were made. In the action, we seek compensatory damages in the amount of $500,000 plus statutory interest, punitive damages as well as an award of attorney's fees and costs. One of Spectra's counterclaims was dismissed by the court in response to our motion for summary judgment. The trial was completed in February 2005. The jury returned a verdict and judgment in our favor in the amount of approximately $600,000. . We have filed a notice of appeal with respect to the damages portion of the verdict. On June 1, 2005, Spectra voluntarily dismissed with prejudice its remaining pending counterclaim against us. We have entered into an escrow agreement with the defendants pursuant to which approximately $600,000 representing the amount of the judgment has been deposited. Withdrawal of the funds will be permitted only upon the date that judgment in the matter becomes a final, non-appealable decision, or earlier upon the written agreement of all parties.

We are the respondent in an arbitration proceeding filed on December 10, 2002 captioned J. Terrence Feeley v. Infinite Group, Inc. Claimant, a former employee and former member of our board of directors, alleges that the parties entered into a consulting agreement dated June 27, 2002 relative to the early termination of claimant's employment requiring certain cash payments to be made. Claimant alleges that we have failed or refused to make such cash payments and have breached the agreement and seeks all monies owed to him, said amount

alleged to be approximately $130,000. We answered the claim by admitting that a letter agreement was entered into but denied all of the remaining allegations. We also filed a counterclaim in the arbitration proceeding. We filed a related claim against Mr. Feeley in the Superior Court, State of Rhode Island on September 5, 2003. We claim that he breached certain provisions of his employment agreement, breached fiduciary duties he owed to us and violated several provisions of the June 27, 2002 letter agreement. We seek compensatory damages in amounts to be shown at trial, and preliminary and permanent injunctive relief and other relief as may be appropriate.

Mr. Feeley's arbitration claims are pending before the American Arbitration Association and an arbitrator selected by the parties. Our claims against Mr. Feeley are pending in the Rhode Island Superior Court. In January of 2004, the parties agreed to stay arbitration proceedings and to mediate all the disputes under procedures available through the Superior Court. To date, neither party has initiated mediation proceedings.

Other than the foregoing proceeding, we are not a party to any material legal proceeding.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds.

Recent Sales of Unregistered Securities

For the three months ended March 31, 2004, we issued 2,120,000 restricted shares of common stock at $.05 per share in private placement transactions. In addition we issued 1,500,000 restricted shares of common stock to employees as compensation, which were valued at .05 per share.

These transactions were exempt from registration, as they were nonpublic offerings made pursuant to Sections 4(2) and 4(6) of the Act. All shares issued in the transactions described hereinabove bore an appropriate restrictive legend.

Item 3.Defaults Upon Senior Securities.

The Company's LF subsidiary had a $1,250,000 bank term promissory note that required monthly principal and interest payments amounting to approximately $13,000 through February 2011. The outstanding balance as of March 31, 2004 amounted to $767,547 and bore interest at the bank's prime rate plus 1.0%. All the assets of LF and the guarantee of the Company secured the note. We continued to be in violation of certain loan covenants. These violations related to exceeding certain levels of the ratio of debt to intangible net worth, not meeting the minimum current ratio or the working capital ratio, and exceeding capital expenditure limits. Accordingly, the entire outstanding portion of the note was classified as current.

The Company's LF subsidiary had a $1,260,000 bank term promissory note that required monthly principal and interest payments amounting to approximately $13,000 through December 2014. The outstanding balance as of March 31, 2004 amounted to $1,028,844 and bore interest at the bank's prime rate plus .75%. We continued to be in violation of certain covenants under the term of this note. Accordingly, the entire outstanding portion of the note was classified as current.

The Company's LF subsidiary was obligated under a capital lease for the LF operating facility. The lease provides for monthly payments to an escrow account in amounts sufficient to allow for the repayment of the principal of the

underlying tax-exempt bonds together with interest at 7.25% through June 2012. The outstanding balance as of March 31, 2004 amounted to $485,000. Annual payments of principal were $40,000 for fiscal 2004 and increased by $5,000 annually through June 2012. Under the terms of this capital lease, the Company was prohibited from paying dividends or making other cash distributions. According to the terms of the lease agreement, the Company was required to comply with certain covenants. We continued to be in violation of these covenants. Accordingly, the entire outstanding portion of this obligation was classified as current.

The aggregate amount of the aforementioned notes payable and capital lease obligations classified as current liabilities was $2,281,391 at March 31, 2004.

Item 4. Submission of Matters to a Vote of Security Holders.

None.

Item 5. Other Information.

None.

Item 6. Exhibits.

a. Exhibits:

Exhibit No.	Description
31.1	Certification of Chief Executive Officer and Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Certification of Chief Executive Officer and Chief Executive Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

SIGNATURES

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

Infinite Group Inc.

(Registrant)

Date July 26, 2005 /s/ Michael S. Smith
Chief Executive Officer

Date July 26, 2005 /s/ Michael S. Smith
Chief Financial Officer
(Principal Financial Officer)