INFINITE GROUP INC
Form 10-Q
November 10, 2010

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

FORM 10-Q

(Mark One)

x QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 For the quarterly period ended: September 30, 2010

¨ TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from _________ to __________

Commission file number: 0-21816

INFINITE GROUP, INC.
(Exact name of registrant as specified in its charter)

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

60 Office Park Way
Pittsford, New York 14534
(Address of principal executive offices)
(Zip Code)

(585) 385-0610
(Registrant's telephone number, including area code)

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

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 required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.
Yes x 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 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. (Check one):

Large Accelerated filer ¨ Accelerated filer ¨
Non-accelerated filer (Do not check if a smaller reporting company) ¨ Smaller reporting company x

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.
There were 26,461,883 shares of the issuer’s common stock, par value $.001 per share, outstanding as of November 10, 2010.

INFINITE GROUP, INC.

FORM 10-Q REPORT

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FORWARD-LOOKING STATEMENTS

Certain statements made in this Quarterly Report on Form 10-Q are "forward-looking statements" 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. We undertake no obligation to revise or update publicly any forward-looking statements for any reason. 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. Consolidated Financial Statements

INFINITE GROUP, INC.

Consolidated Balance Sheets

	September 30, 2010 (Unaudited)	December 31, 2009
ASSETS		
Current assets:		
Cash	$ 104,462	$ 196,711
Accounts receivable, net of allowance of $70,000	665,780	1,118,580
Prepaid expenses and other current assets	65,732	56,622
Total current assets	835,974	1,371,913
Property and equipment, net	76,265	58,777
Deposits and other assets	18,424	21,544
Total assets	$ 930,663	$ 1,452,234
LIABILITIES AND STOCKHOLDERS' DEFICIENCY		
Current liabilities:		
Accounts payable	$ 587,845	686,457
Accrued payroll	368,056	388,131
Accrued interest payable	291,496	275,563
Accrued retirement and pension	3,443,450	3,078,361
Accrued expenses - other	39,197	61,632
Current maturities of long-term obligations-bank	41,869	32,243
Notes payable	470,000	295,000
Notes payable - related parties	174,000	154,000
Total current liabilities	5,415,913	4,971,387
Long-term obligations:		
Notes payable:		
Banks and other	172,939	334,029
Related parties	501,324	501,324
Accrued pension expense	735,012	735,012
Total liabilities	6,825,188	6,541,752
Commitments and contingencies (Note 5)		
Stockholders' deficiency:		
Common stock, $.001 par value, 60,000,000 shares authorized; 26,461,883 (25,661,883 – 2009) shares issued and outstanding	26,461	25,661
Additional paid-in capital	29,988,220	29,870,506

Accumulated deficit	(33,104,166)	(32,180,645)
Accumulated other comprehensive loss	(2,805,040)	(2,805,040)
Total stockholders' deficiency	(5,894,525)	(5,089,518)
Total liabilities and stockholders' deficiency	$ 930,663	$ 1,452,234

See notes to unaudited consolidated financial statements.

INFINITE GROUP, INC.

Consolidated Statements of Operations (Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2010	2009	2010	2009
Sales	$ 2,212,716	$ 2,756,463	$ 7,206,004	$ 8,320,492
Cost of services	1,589,069	2,065,766	5,354,738	6,344,445
Gross profit	623,647	690,697	1,851,266	1,976,047
Costs and expenses:				
General and administrative	311,997	306,425	928,125	918,633
Defined benefit pension plan	126,675	133,468	372,624	430,214
Selling	383,633	416,656	1,264,680	1,309,795
Total costs and expenses	822,305	856,549	2,565,429	2,658,642
Operating loss	(198,658)	(165,852)	(714,163)	(682,595)
Interest expense:				
Related parties	(13,838)	(21,060)	(38,515)	(62,423)
Other	(58,332)	(50,130)	(169,613)	(155,533)
Total interest expense	(72,170)	(71,190)	(208,128)	(217,956)
Loss before income tax expense	(270,828)	(237,042)	(922,291)	(900,551)
Income tax expense	-	-	(1,230)	(4,000)
Net loss	$ (270,828)	$ (237,042)	$ (923,521)	$ (904,551)
Net loss per share – basic and diluted	$ (.01)	$ (.01)	$ (.04)	$ (.04)
Weighted average number of shares outstanding – basic and diluted	26,148,840	25,498,253	25,825,986	25,400,155

See notes to unaudited consolidated financial statements.

INFINITE GROUP, INC.

Consolidated Statements of Cash Flows (Unaudited)

	Nine Months Ended September 30, 2010	Nine Months Ended September 30, 2009
Operating activities:		
Net loss	$ (923,521)	$ (904,551)
Adjustments to reconcile net loss to net cash used by operating activities:		
Stock based compensation	78,514	118,580
Depreciation	26,265	23,568
Decrease (increase) in assets:		
Accounts receivable	452,800	(99,659)
Other assets	(5,990)	(19,535)
(Decrease) increase in liabilities:		
Accounts payable	(98,612)	174,780
Accrued expenses	13,423	268,550
Accrued pension and retirement	365,089	376,316
Net cash used by operating activities	(92,032)	(61,951)
Investing activities:		
Purchase of property and equipment	(5,078)	(6,651)
Net cash used by investing activities	(5,078)	(6,651)
Financing activities:		
Repayments of notes payable	(15,139)	(31,197)
Proceeds from note payable - related parties	90,000	76,151
Repayments of note payable - related parties	(70,000)	(76,151)
Proceeds from exercise of stock options	-	1,750
Net cash provided by (used by) financing activities	4,861	(29,447)
Net decrease in cash and cash equivalents	(92,249)	(98,049)
Cash - beginning of period	196,711	153,336
Cash - end of period	$ 104,462	$ 55,287
Supplemental disclosure:		
Cash paid for:		
Interest	$ 154,082	$ 173,790
Income taxes	$ 1,230	$ 4,000

See accompanying notes to unaudited consolidated financial statements.

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 (U.S.) for interim financial information and with instructions to Form 10-Q. Accordingly, they do not include all of the information and footnotes required by accounting principles generally accepted in the U.S. 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 the notes thereto included in the Company's Annual report on Form 10-K for the year ended December 31, 2009 filed with the U.S. Securities and Exchange Commission (SEC). Results of consolidated operations for the three and nine months ended September 30, 2010 are not necessarily indicative of the operating results that may be expected for the year ending December 31, 2010. The unaudited consolidated financial statements herein include the accounts of the Company and its wholly owned subsidiaries. The subsidiaries are inactive. All material inter-company accounts and transactions have been eliminated.

Note 2. Summary of Significant Accounting Policies

There are several accounting policies that the Company believes are significant to the presentation of its consolidated financial statements. These policies require management to make complex or subjective judgments about matters that are inherently uncertain. Note 3 to the Company's audited consolidated financial statements for the year ended December 31, 2009 presents a summary of significant accounting policies.

Reclassification

The Company reclassified certain prior year amounts in its consolidated financial statements to conform to the current year's presentation.

Recent Accounting Pronouncements

In July 2010, the FASB issued ASU 2010-20, "Disclosures about the Credit Quality of Financing Receivables and the Allowance for Credit Losses". The new disclosure guidance will expand the existing requirements and will lead to greater transparency into a company's exposure to credit losses from lending arrangements. The extensive new disclosures of information as of the end of a reporting period will become effective for both interim and annual reporting periods ending on or after December 15, 2010. Specific disclosures regarding activity that occurred before the issuance of the ASU, such as the allowance roll-forward and modification disclosures, will be required for periods beginning on or after December 15, 2010. The Company is currently assessing the impact that ASU 2010-20 will have on its consolidated financial statements.

Effective January 1, 2010, the Company partially adopted the provisions of FASB ASU No. 2010-06, "Improving Disclosures about Fair Value Measurements," which amends ASC 820-10-50 to require new disclosures concerning (1) transfers into and out of Levels 1 and 2 of the fair value measurement hierarchy, and (2) activity in Level 3 measurements. In addition, ASU No. 2010-06 clarifies certain existing disclosure requirements regarding the level of disaggregation and inputs and valuation techniques and makes conforming amendments to the guidance on employers' disclosures about postretirement benefit plans assets. The requirements to disclose separately purchases, sales,

issuances, and settlements in the Level 3 reconciliation are effective for fiscal years beginning after December 15, 2010 (and for interim periods within such years). Accordingly, the Company will apply the disclosure requirements relative to the Level 3 reconciliation in the first quarter of 2011. There was no impact on the Company's financial position, results of operations or cash flows as a result of the partial adoption of ASU No. 2010-06 as of and for the nine months ended September 30, 2010.

Management does not believe that any other recently issued, but not yet effective accounting standard if currently adopted would have a material effect on the accompanying consolidated financial statements.

Note 3. Stock Option Plans

The Company has approved stock options plans covering up to an aggregate of 9,172,933 shares of common stock. Such options may be designated at the time of grant as either incentive stock options or nonqualified stock options. Stock based compensation includes expense charges related to all stock-based awards to employees, directors and consultants. Such awards include options, warrants and stock grants.

The fair value of each option granted is estimated using the Black-Scholes option-pricing model. The following assumptions were used for the nine months ended September 30, 2010 and 2009.

	2010	2009
Risk-free interest rate	1.73% - 2.93%	2.09% - 2.80%
Expected dividend yield	0%	0%
Expected stock price volatility	75%	75%
Expected life of options	5.75 years	5.75 years

The Company recorded expense for options and warrants issued to employees and independent service providers for the three months and nine months ended September 30, 2010 and 2009 as follows. There was no impact on net loss per share for the three or nine months ended September 30, 2010 and 2009.

	Three Months ended September 30, 2010	Three Months ended September 30, 2009	Nine Months ended September 30, 2010	Nine Months ended September 30, 2009
Employee stock options	$ 19,598	$ 29,689	$ 78,514	$ 120,749
Consultants – common stock warrants	-	-	-	(2,169)
Total expense	$ 19,598	$ 29,689	$ 78,514	$ 118,580

A summary of all stock option activity for the nine months ended September 30, 2010 follows:

	Number of Options	Weighted Average Exercise Price	Weighted-Average Remaining Contractual Term	Aggregate Intrinsic Value
Outstanding at December 31, 2009	5,491,500	$ .26		
Options granted	1,766,000	$ .14		
Options expired	(558,000)	$ .29		
Outstanding at September 30, 2010	6,699,500	$ .24	6.3 years	$ 21,860
Exercisable at September 30, 2010	4,800,834	$ .26	5.0 years	$ 21,860

The weighted average fair value of options granted during the nine months ended September 30, 2010 was approximately $.09 ($.12 during the nine months ended September 30, 2009). Options for 25,000 shares were exercised during the nine months ended September 30, 2009 with aggregate proceeds to the Company of $1,750. The options had an intrinsic value of $ 8,250. No options were exercised during 2010.

A summary of nonvested stock option activity for the nine months ended September 30, 2010 follows:

	Number of Nonvested Options	Weighted Average Fair Value at Grant Date
Nonvested outstanding at December 31, 2009	866,333	$ .15
Options granted	1,766,000	$ .09
Options vested	(542,000)	$ .26
Options forfeited	(191,667)	$ .13
Nonvested outstanding at September 30, 2010	1,898,666	$ .10

At September 30, 2010, there was approximately $146,500 of total unrecognized compensation cost related to non-vested options granted under the Company's stock option plans. That cost is expected to be recognized over a weighted average period of two years. The total fair value of shares that vested during the nine months ended September 30, 2010 was approximately $142,000.

Note 4. Earnings Per Share

Basic net income (loss) per share is based on the weighted average number of common shares outstanding during the periods presented. Diluted net 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 stock options, stock warrants and convertible notes payable. 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 and warrants assumed to be exercised. In a loss period, the calculation for basic and diluted net loss per share is considered to be the same, as the impact of potential common shares is anti-dilutive.

As of September 30, 2010, convertible debt, options and warrants to purchase 25,061,128 shares of common stock (23,206,079 as of September 30, 2009) that could potentially dilute basic net income per share in the future were excluded from the calculation of diluted net income (loss) per share because their inclusion would have been anti-dilutive.

Note 5. Employee Pension Plan

Prior to December 30, 2002, the Company owned 100% of the common stock of Osley & Whitney, Inc. (O&W). On December 30, 2002, the Company sold 100% of the O&W common stock to a third party, but continued to act as the sponsor of the Osley & Whitney, Inc. Retirement Plan (the Plan). Although the Company continued to act as the sponsor of the Plan after the sale, during 2007 management determined that it had no legal obligation to do so.

During 2007, the Company submitted information to the Department of Treasury (Treasury) advocating that it had no legal obligation to act as the sponsor of the Plan to ascertain whether the Treasury concurred or disagreed with this position. The Company subsequently provided responses to Treasury inquiries related to this determination. In October 2009, the Company received a report from the Treasury that stated that the Treasury staff disagreed with the Company's position and as a result, the Company is responsible for excise taxes attributed to the funding deficiency of $1,836,359 for the years 2003 through 2007 which funding deficiency can only be corrected by contributing $1,836,359 to the Plan. The report also states that proposed 10% excise taxes of $348,500, penalties for late payment of excise taxes of approximately $1,200,000, and 100% excise taxes of approximately $3,500,000 related to the years ended December 31, 2006 and 2007 may be imposed. Penalties for late payment may be removed if the Company provides reasonable cause for not paying the excise taxes and the Treasury concurs with the Company's position. The Company and its outside legal counsel disagree with significant aspects of both the factual findings and legal conclusions set forth in the report and, in accordance with Treasury procedures, have responded with a detailed analysis of its opposition to their findings. The Company plans to diligently pursue all appropriate steps to perfect its appeal rights and attempt to prevail on the merits of its position, which will include filing a protest, requesting an appeals conference, and, if needed, petitioning the tax court and advocating its position in that forum.

If the Company does not ultimately prevail, it will become obligated for Plan contributions of approximately $2.2 million as of September 30, 2010 and 10% excise taxes on accumulated unfunded Plan contributions for the Plan years ended December 31, 2006 and 2007 of approximately $348,500, as stated above, and potentially additional 10% excise taxes of approximately $220,000 for the year ended December 31, 2008, which have not been accrued based upon the Company's determination that it has no legal obligation to act as the Plan sponsor and the Company's belief that the likelihood is not probable that it will be required to pay these excise taxes. Further, if the Company does not

ultimately prevail, it may be required to pay interest on these excise taxes and potentially incur penalties for late payment of excise taxes and additional excise taxes up to 100% of each year's required funding deficiency. The Company has accrued amounts related to excise taxes, including late fees and interest, on unfunded contributions for 2003, 2004 and 2005 of approximately $463,000 as of September 30, 2010 ($445,000 at December 31, 2009). No excise taxes, late fees or interest for 2006, 2007, 2008, and 2009 has been accrued at September 30, 2010 or December 31, 2009. The Company does not have the funds available to make required contributions which approximate $2.2 million and does not intend to make any contributions to the Plan during 2010.

During 2006, the Pension Benefit Guarantee Corporation (PBGC) placed a lien on all of the Company's assets to secure the contributions due to the Plan. This lien is subordinate to liens that secure accounts receivable financing and certain notes payable.

On April 29, 2009, acting for the Plan, the Company sent the Plan participants a notice of intent to terminate the Plan in a distress termination. The Company also provided additional documentation regarding the Company's status and the status of the Plan. The termination of the Plan is subject to approval by the PBGC. During 2009, the Company provided information to the PBGC which Company management believes satisfies the requirements of the PBGC. During August 2010, the PBGC requested additional information and the Company provided its response.

At September 30, 2010, the Plan had an accrued pension obligation liability of approximately $4,040,000 ($3,696,640 at December 31, 2009), which includes the underfunded amount plus interest on past due payments and excise taxes including penalties and interest of approximately $463,000. Accumulated other comprehensive loss of $2,805,040 at September 30, 2010 has been recorded as a reduction of stockholders' deficiency.

The market value of the Plan assets decreased from $2,004,117 at December 31, 2009 to $1,654,563 at September 30, 2010. The decrease was comprised of investment gains of $20,663, benefit payments of $335,556 and expenses of $34,661.

Net periodic pension cost recorded in the accompanying statements of operations includes the following components of expense (benefit) for the periods presented.

	Three Months ended September 30, 2010	Three Months ended September 30, 2009	Nine Months ended September 30, 2010	Nine Months ended September 30, 2009
Interest cost	$ 72,531	$ 71,996	$ 217,594	$ 215,989
Expected return on plan assets	(39,148)	(42,115)	(117,443)	(126,346)
Service cost	12,500	17,750	37,500	53,250
Actuarial loss	31,882	37,343	95,645	112,030
Net periodic pension cost	$ 77,765	$ 84,974	$ 233,296	$ 254,923

Note 6. Supplemental Cash Flow Information

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

	Nine Months Ended September 30,	
	2010	2009
Conversion of accrued interest payable under note payable -related party into 800,000 and 500,000 shares on common stock, respectively	$ 40,000	$ 25,000
Purchase of computer and communications equipment through long-term obligations	$ 38,675	$ 9,465
Conversion of convertible accrued interest payable into a convertible note payable	$ -	$ 25,000

During the nine months ended September 30, 2009, warrants were exercised for 60,000 shares of common stock on a cashless basis resulting in the Company's net issuance of 23,265 shares of common stock. During 2010, no options or warrants were exercised.

Note 7. Notes Payable

During the nine months ended September 30, 2010, the Company entered into the following note payable agreements and made principal payments as follows.

On August 13, 2010, the Company borrowed $40,000 under the terms of a demand note payable to a member of the Company's board of directors with interest at 12% annually. At the option of the holder, the principal is convertible

into shares of common stock at the rate of $.11 per share.

On May 27, 2010, the Company borrowed $50,000 under the terms of a demand note payable to the Company's President with interest at 12% annually. Principal of $45,000 was repaid through September 30, 2010. In addition, through September 30, 2010, $25,000 of principal was repaid on other notes payable to the Company's President.

During the first quarter of 2010, the Company financed the acquisition of computer and communications equipment of $38,675 under the terms of capital leases with payments aggregating $1,365 per month due over 36 months.

Note 8. Related Party Transactions

On September 1, 2010, Mr. Donald W. Upson, the Company's chairman of the board of directors, became an employee of the Company with the title of Federal Business Strategist and receives a salary and employee benefits according to the Company's standard policies. As disclosed in note 12 to the Company's audited consolidated financial statements for the year ended December 31, 2009, Mr. Upson previously was a consultant to the Company performing the same services on a month to month basis and earning $9,600 per month.

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

IT Consulting

We are a provider of IT services to federal, state and local government and commercial clients. Our expertise includes managing leading edge operations and implementing complex programs in advanced server management, data center consolidation, virtualization services (including server, desktop, application, and storage), cloud computing, information security, wireless technology, human capital services, business and technology integration, and enterprise architecture. We focus on aligning business processes with technology for delivery of solutions meeting our clients' exact needs and providing expert management services to the lifecycle of technology-based projects. We have business development personnel headquartered from our corporate office in Pittsford, NY, as well as business development offices in the Washington, D.C. metropolitan area and Colorado Springs, CO. During 2010, we have expanded our business operations and expect to have future sales prospects in the State of Mississippi. We also increased our marketing focus to include providing IT consulting services to middle market sized businesses in Upstate New York, nearby our corporate headquarters, and in the Denver/Colorado Springs region, where we have approximately 50 employees and have provided IT services for several years.

We have several contract vehicles that enable us to deliver a broad range of our services and solutions to the U.S. Government and the State of Mississippi. The quality and consistency of our services and IT expertise allow us to maintain long-term relationships with our major clients. We have entered into various subcontract agreements with prime contractors to the U.S. Government, state and local governments and commercial customers.

Results of Operations

Comparison of Three and Nine Month Periods ended September 30, 2010 and 2009

The trends suggested by the following tables are not indicative of future operating results. The following table compares our statements of operations data for the three months ended September 30, 2010 and 2009.

	Three Months Ended September 30,					
					2010 vs. 2009	
	2010	As a % of Sales	2009	As a % of Sales	Amount of Change	% Increase (Decrease)
Sales	$ 2,212,716	100.0%	$ 2,756,463	100.0%	$ (543,747)	(19.7)%
Cost of services	1,589,069	71.8	2,065,766	74.9	(476,697)	(23.1)
Gross profit	623,647	28.2	690,697	25.1	(67,050)	(9.7)
General and administrative	311,997	14.1	306,425	11.1	5,572	1.8

Defined benefit pension plan		126,675	5.7		133,468	4.8		(6,793)	(5.1)
Selling		383,633	17.3		416,656	15.1		(33,023)	(7.9)
Total costs and expenses		822,305	37.2		856,549	31.0		(34,244)	(4.0)
Operating loss		(198,658)	(9.0)		(165,852)	(5.9)		32,806	19.8
Interest expense		(72,170)	(3.3)		(71,190)	(2.6)		980	1.4
Net loss	$	(270,828)	(12.2)%	$	(237,042)	(8.6)%	$	33,786	14.3%
Net loss per share - basic and diluted	$	(.01)		$	(.01)		$	-	

The following table compares our statements of operations data for the nine months ended September 30, 2010 and 2009.

	2010	As a % of Sales	2009	As a % of Sales	2010 vs. 2009 Amount of Change	% Increase (Decrease)
Sales	$ 7,206,004	100.0%	$ 8,320,492	100.0%	$ (1,114,488)	(13.4)%
Cost of services	5,354,738	74.3	6,344,445	76.3	(989,707)	(15.6)
Gross profit	1,851,266	25.7	1,976,047	23.7	(124,781)	(6.3)
General and administrative	928,125	12.9	918,633	11.0	9,492	1.0
Defined benefit pension plan	372,624	5.2	430,214	5.2	(57,590)	(13.4)
Selling	1,264,680	17.6	1,309,795	15.7	(45,115)	(3.4)
Total costs and expenses	2,565,429	35.6	2,658,642	32.0	(93,213)	(3.5)
Operating loss	(714,163)	(9.9)	(682,595)	(8.2)	31,568	4.6
Interest expense	(208,128)	(2.9)	(217,956)	(2.6)	(9,828)	(4.5)
Income tax expense	(1,230)		(4,000)		(2,770)	(69.3)
Net loss	$ (923,521)	(12.8)%	$ (904,551)	(10.9)%	$ 18,970	2.1%
Net loss per share - basic and diluted	$ (.04)		$ (.04)		$ .00	

Sales

Sales for the three months ended September 30, 2010 were $2,212,716 a decrease of $543,747 or 19.7% as compared to sales for the three months ended September 30, 2009 of $2,756,463. Sales for the nine months ended September 30, 2010 were $7,206,004, a decrease of $1,114,488 or 13.4% as compared to sales for the nine months ended September 30, 2009 of $8,320,492. The decrease primarily results from the completion of certain U.S. government assignments and certain projects for other clients that were not offset by the addition of new projects and assignments. Our Microsoft Stimulus360 project for a state government client was also completed during June 2010. Stimulus360 is a Microsoft solution used to help public sector agencies track, measure, and share information about federal stimulus programs through easy to use graphical dashboards and maps. Our work for this state government continued when a new project with an approximate six month duration started in July 2010.

Cost of Services and Gross Profit

Cost of services represents the cost of employee services related to our sales. Cost of services for the three months ended September 30, 2010 was $1,589,069 or 71.8% of sales as compared to $2,065,766 or 74.9% of sales for the three months ended September 30, 2009. Gross profit was $623,647 or 28.2% of sales for the three months ended September 30, 2010 compared to $690,697 or 25.1% of sales for the three months ended September 30, 2009. Cost of services for the nine months ended September 30, 2010 was $5,354,738 or 74.3% of sales as compared to $6,344,445 or 76.3% of sales for the nine months ended September 30, 2009. Gross profit was $1,851,266 or 25.7% of sales for the nine months ended September 30, 2010 compared to $1,976,047 or 23.7% of sales for the nine months ended September 30, 2009.

The increase in gross profit margin percent is due to a change in the mix of our business resulting from new projects in 2010 which carried higher profit margins than work completed in 2009. Our personnel utilization rates also improved during the most recent quarter.

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 September 30, 2010 were $311,997 which was an increase of $5,572 or 1.8% as compared to $306,425 for the three months ended September 30, 2009. As a percentage of sales, general and administrative expense was 14.1% for the three months ended September 30, 2010 and 11.1% for the three months ended September 30, 2009.

General and administrative expenses for the nine months ended September 30, 2010 increased by $9,492 or 1.0% from $918,633 for the nine months ended September 30, 2009 to $928,125 for the nine months ended September 30, 2010. As a percentage of sales, general and administrative expenses were 12.9% for the nine months ended September 30, 2010 and 11.0% for the nine months ended September 30, 2009.

General and administrative expenses in 2010 were not significantly different from 2009. We anticipate that general and administrative expenses will increase as we work to grow our business and incur travel and other expenses associated with managing a larger business.

Defined Benefit Pension Plan Expenses

Defined benefit pension plan expenses include expenses (including pension expense, professional services, and interest costs) associated with the Osley & Whitney, Inc. Retirement Plan (the Plan) of $126,675 for the three months ended September 30, 2010 and $133,468 for the three months ended September 30, 2009, a decrease of $6,793. We incurred expenses of $372,625 and $430,214 for the nine months ended September 30, 2010 and 2009, a decrease of $57,590.

During the nine months ended September 30, 2010, we incurred legal and professional fees of approximately $29,600 in connection with compliance requirements and advocating our legal position in response to a request for additional information from the Pension Benefit Guarantee Corporation ("PBGC") in August 2010 as compared to approximately $69,300 for the nine months ended September 30, 2009. Net periodic pension cost decreased by $21,600 to $233,300 for the nine months ended September 30, 2010 due principally to changes in pension regulations. We continue to accrue interest and fees on unpaid excise taxes for plan years 2003, 2004 and 2005, as well as interest on unfunded contributions, which amounted to additional expense of approximately $109,700 and $106,000 for the nine months ended September 30, 2010 and 2009, respectively.

Selling Expenses

For the three months ended September 30, 2010, we incurred selling expenses of $383,633 as compared to $416,656 for the three months ended September 30, 2009, a decrease of $33,023 or 7.9%. For the nine months ended September 30, 2010 we incurred selling expenses of $1,264,680 compared to $1,309,795 for the nine months ended September 30, 2009, a decrease of $45,115 or 3.4%.

The decrease for the three and nine months ended September 30, 2010 is principally due to the reduction of two positions in April 2010 in our sales and business development personnel.

Operating Loss

For the three months ended September 30, 2010, our operating loss was $(198,658) compared to an operating loss of $(165,852) for the three months ended September 30, 2009, an increase in the loss of $32,806. This is principally attributable to a reduction in sales of $543,747, which was partially offset by decreases in cost of services and operating expenses of $476,697 and $34,244, respectively.

For the nine months ended September 30, 2010 our operating loss increased to $(714,163) compared to an operating loss of $(682,595) for the nine months ended September 30, 2009, an increase in the loss of $31,568. This is principally attributable to a decrease in gross profit of $124,781 or 6.3% offset by a decrease in operating expenses of $93,213 or 3.5%.

Interest Expense

Interest expense includes interest on indebtedness and fees for financing accounts receivable invoices. Interest expense was $72,170 for the three months ended September 30, 2010 compared to interest expense of $71,190 for the three months ended September 30, 2009. Interest expense was $208,128 for the nine months ended September 30, 2010 compared to interest expense of $217,956 for the nine months ended September 30, 2009.

Related party interest expense increased by $793 and decreased by $123 for the three and nine month periods ended September 30, 2010 as compared to the three and nine month periods ended September 30, 2009. We incurred additional short-term borrowings from related parties beginning in August 2010.

Other interest expense increased by $187 and decreased by $9,705 for the three and nine month periods ended September 30, 2010, respectively, as compared to the three and nine month periods ended September 30, 2009. Our fees for financing accounts receivable were reduced beginning in June 2009, thereby reducing our interest expense.

Income Taxes

Income tax expense was $0 for the three months ended September 30, 2010 and 2009, respectively. Income tax expense was $1,230 and $4,000 for the nine months ended September 30, 2010 and 2009, respectively, consisting of state taxes.

Net Loss

For the three months ended September 30, 2010, we recorded a net loss in the amount of $(270,828) or $(.01) per share compared to a net loss of $(237,042) or $(.01) per share for the three months ended September 30, 2009. For the nine months ended September 30, 2010, we recorded a net loss in the amount of $(923,521) or $(.04) per share compared to a net loss of $(904,551) or $(.04) per share for the nine months ended September 30, 2009.

Stock-Based Compensation

For the nine months ended September 30, 2010 and 2009, we recorded expense of $78,514 and $118,580, respectively, for stock options expense issued to employees and board members and equity instruments issued to consultants.

Liquidity and Capital Resources

At September 30, 2010, we had cash of $104,462 available for our working capital needs and planned capital asset expenditures. Our primary liquidity needs are the financing of working capital and capital expenditures. Our primary source of liquidity is cash provided by operations and our factoring line of credit. At September 30, 2010, we had financing availability, based on eligible accounts receivable, of $126,000 under this line.

At September 30, 2010, we had a working capital deficit of approximately $4.6 million and a current ratio of .15. Our objective is to improve our working capital position from profitable operations. The Plan's current liabilities have a significant impact on our working capital. Without the current liabilities of the Plan of approximately $3.3 million, our working capital deficit would have been approximately $1.3 million.

During 2010 and 2009, we financed our business activities through the issuance of notes payable to third parties, sales with recourse of our accounts receivable, and capital equipment leases. Also, during 2010 and 2009, a certain related party note holder converted principal and accrued interest payable into shares of our common stock. During May and August 2010, we received an aggregate of $90,000 through working capital loans from our president and from one of our directors of which principal of $45,000 were repaid through September 30, 2010. In addition, through September 30, 2010, $25,000 of principal was repaid on certain other notes payable to our president. We have used our common stock and common stock options and warrants to provide compensation to certain employees and consultants and to fund liabilities.

In June 2008, we received $200,000 through a working capital loan from a third party, which balance was reduced to $175,000 during 2009 and matures on January 1, 2011. We have notes payable of $265,000 which mature on December 31, 2010. We plan to renegotiate the terms of these notes payable, included in current liabilities, or seek funds to replace these notes payable. We have short-term notes payable to related parties which proceeds were used for working capital. Our borrowings under our accounts receivable financing line change based on cash required to fund accounts payable and accrued payrolls relative to the timing of cash received from the payment of client invoices.

We believe the capital available under our factoring line of credit, from related party loans, and cash generated by improving the results of our operations provide sources to fund our ongoing operations and to support the internal growth we expect to achieve for at least the next 12 months. If we do not improve the results of our operations in future periods, we expect that additional working capital will be required to fund our business. Although we have no assurances, we believe that related parties are one source that will continue to provide working capital loans to us on similar terms, as in the past, as may be necessary to fund our on-going operations for at least the next 12 months. If we experience significant growth in our sales, we believe that this may require us to increase our financing line or obtain

additional working capital from other sources to support our sales growth. There is no assurance that in the event we need additional funds that adequate additional working capital will be available or, if available, will be offered on acceptable terms.

We anticipate financing our external growth from acquisitions and our longer-term internal growth through one or more of the following sources: cash from operations; additional borrowing; issuance of equity; use of our existing revolving credit facility; or a refinancing of our credit facilities.

We do not have the funds available to make required contributions to the Plan which approximate $2.2 million or intend to make any contributions to the Plan during 2010.

The following table sets forth our sources and uses of cash for the periods presented:

	Nine Months Ended September 30,	
	2010	2009
Net cash used by operating activities	$ (92,032)	$ (61,951)
Net cash used by investing activities	(5,078)	(6,651)
Net cash provided/(used) by financing activities	4,861	(29,447)
Net decrease in cash	$ (92,249)	$ (98,049)

Cash Flows from Operating Activities

During the nine months ended September 30, 2010, cash used in operations was $92,032 compared with cash used in operations of $61,951 for the nine months ended September 30, 2009. Our operating cash flow is primarily affected by the overall profitability of our contracts, our ability to invoice and collect from our clients in a timely manner, and our ability to manage our vendor payments. We have focused on improving our employee utilization rates during 2010 to improve our gross profit margin. We bill our clients weekly or monthly after services are performed, depending on the contract terms. Our accounts receivable decreased principally due to the decline in sales in the 2010 period. The increase in liabilities is primarily due to increased accrued pension and retirement expenses offset by a decrease in accounts payable and accrued expenses.

Cash Flows from Investing Activities

Cash used by investing activities for the nine months ended September 30, 2010 was $5,078 compared with $6,651 for the nine months ended September 30, 2009. Cash used in investing activities was primarily for capital expenditures for computer hardware and software. We do not have any plans for significant capital expenditures in the near future.

Cash Flows from Financing Activities

During the nine months ended September 30, 2010, cash provided by financing activities was $4,861 consisting of $90,000 of proceeds from related party borrowings offset by payments to related parties of $70,000 and principal payments of $15,139 on notes payable. In comparison, for the nine months ended September 30, 2009, cash used by financing activities was $31,197 for principal payments on notes payable offset by proceeds from the exercise of common stock options of $1,750.

Credit Agreement

We have secured an accounts receivable financing line of credit from an independent financial institution that allows us to sell selected accounts receivable invoices to the financial institution with full recourse against us in the amount of $2 million, including a sublimit for one major client of $1.5 million. This provides us with the cash needed to finance certain costs and expenses. At September 30, 2010, we had financing availability, based on eligible accounts receivable, of $126,000 under this line. We pay fees based on the length of time that the invoice remains unpaid.

Future Trends

As discussed above, we believe that our operations, as currently structured, together with our available financial resources, will result in improved financial performance in future periods. However, we do not have the funds available to make required contributions to the Plan which approximate $2.2 million or intend to make any contributions to the Plan during 2010.

There is no assurance, that our current resources or cash flow from operations will be adequate to fund the liabilities under the Plan if the Treasury does not concur with our position or that we will be successful in raising additional working capital when necessary. Our failure to raise necessary working capital could force us to curtail operations, which would have a material adverse effect on our financial condition and results of operations.

The current recessionary economy may impact certain portions of our business and our growth opportunities as certain projects are deferred pending funding or improved economic conditions. However, one of our major sources of revenue is from ongoing data center support which is critical to the operation of our clients and is not solely dependent upon current economic factors. Our focus areas include virtualization and data center projects which are based on our clients' need to upgrade or centralize their data centers and such projects provide a rate of return that justifies these projects. We have Microsoft Gold Partner status, are a VMware Authorized Consultant (VAC), a VMware Enterprise Partner and a VMware Lighthouse Partner, and are a member of the Hewlett Packard Approved Supplier List (ASL), which we believe provide us with a competitive advantage versus those companies that do not have such qualifications and bid against us on certain projects. In November 2009, we entered into master services relationship and authorized reseller agreements with Dell, Inc. Under the master services agreement with Dell's professional services organization, we can rapidly engage on consulting projects and deliver service in a streamlined and efficient manner. Our key areas of focus for our Dell partnership include virtualization services, as well as operational support for major Dell contracts in the federal and defense markets.

During 2010, the U.S. and worldwide capital and credit markets have continued to experience significant price volatility, dislocations and liquidity disruptions, which have caused market prices of many stocks to fluctuate substantially and the spreads on prospective debt financings to widen considerably. These circumstances have materially impacted liquidity in the financial markets, making terms for certain financings less attractive, and in some cases have resulted in the unavailability of financing. Continued uncertainty in the capital and credit markets may negatively impact our business, including our ability to access additional financing at reasonable terms, which may negatively affect our ability to make future acquisitions or expand our business. If our clients are not able to obtain sufficient financing, the clients could delay their payments to us which would negatively impact our cash flow. A prolonged downturn in the financial markets may cause us to seek alternative sources of potentially less attractive financing, and may require us to adjust our business plan accordingly. These events also may make it more difficult or costly for us to raise capital through the issuance of our debt or equity securities. The disruptions in the financial markets may have a material adverse effect on the market value of our common stock and other adverse effects on our business.

Osley & Whitney, Inc. Retirement Plan

Prior to December 30, 2002, we owned 100% of the common stock of Osley & Whitney, Inc. (O&W). On December 30, 2002, we sold 100% of the O&W common stock to a third party, but continued to act as the sponsor of the Plan. Although we continued to act as the sponsor of the Plan after the sale, during 2007 management determined that it had no legal obligation to do so.

During 2007, we submitted information to the Department of Treasury (Treasury) advocating that we had no legal obligation to act as the sponsor of the Plan to ascertain whether the Treasury concurred or disagreed with this position. We subsequently provided responses to Treasury inquiries related to this determination. In October 2009, we received a report from the Treasury that stated that the Treasury staff disagreed with our position and as a result, we are responsible for excise taxes attributed to the funding deficiency of $1,836,359 for the years 2003 through 2007 which funding deficiency can only be corrected by our contributing $1,836,359 to the Plan. The report also states that proposed 10% excise taxes of $348,500, penalties for late payment of excise taxes of approximately $1,200,000, and 100% excise taxes of approximately $3,500,000 related to the years ended December 31, 2006 and 2007 may be imposed. Penalties for late payment may be removed if we provide reasonable cause for not paying the excise taxes and the Treasury concurs with our position. We and our outside legal counsel disagree with significant aspects of both the factual findings and legal conclusions set forth in the report and, in accordance with Treasury procedures, we have responded with a detailed analysis of our opposition to their findings. We will diligently pursue all appropriate steps to perfect our appeal rights and attempt to prevail on the merits of our position, which will include filing a protest, requesting an appeals conference, and, if needed, petitioning the tax court and advocating our position in that forum.

If we do not ultimately prevail, we will become obligated for Plan contributions of approximately $2.2 million as of September 30, 2010 and 10% excise taxes on accumulated unfunded Plan contributions for the Plan years ended December 31, 2006 and 2007 of approximately $348,500, as stated above, and potentially additional 10% excise taxes of approximately $220,000 for the plan year ended December 31, 2008, which have not been accrued based upon our determination that we have no legal obligation to act as the Plan sponsor and our belief that the likelihood is not probable that we will be required to pay these excise taxes. Further, if we do not ultimately prevail, we may be required to pay interest on these excise taxes and potentially incur penalties for late payment of excise taxes and additional excise taxes up to 100% of each year's required funding deficiency. We have accrued amounts related to excise taxes, penalties and interest on unfunded contributions for 2003, 2004 and 2005 of approximately $463,000 as of September 30, 2010 ($445,000 at December 31, 2009). No excise taxes, penalties or interest for 2006, 2007, 2008, and 2009 have been accrued at September 30, 2010 or December 31, 2009. We do not have the funds available to make required contributions which approximate $2.2 million and do not intend to make any contributions to the Plan during 2010.

During 2006, the PBGC placed a lien on all of our assets to secure the contributions due to the Plan. This lien is subordinate to liens that secure accounts receivable financing and certain notes payable.

On April 29, 2009, acting for the Plan, we sent the Plan participants a notice of intent to terminate the plan in a distress termination. We also provided additional documentation regarding our status and the status of the Plan. The termination of the Plan is subject to approval by the PBGC. During 2009, we provided information to the PBGC which management believes satisfies the requirements of the PBGC. During August 2010, the PBGC requested additional information and we provided our response.

At September 30, 2010, the Plan had an accrued pension obligation liability of approximately $4,040,000 which includes the underfunded amount plus interest on past due payments and excise taxes including penalties and interest of approximately $463,000. Accumulated other comprehensive loss of $2,805,040 at September 30, 2010 has been recorded as a reduction of stockholders' deficiency.

The market value of the Plan assets decreased from $2,004,117 at December 31, 2009 to $1,654,563 at September 30, 2010. The decrease was comprised of investment gains of $20,663, benefit payments of $335,556 and expenses of $34,661.

Item 3. Quantitative and Qualitative Disclosures About Market Risk.

As a smaller reporting company we are not required to provide the information required by this Item.

Item 4. Controls and Procedures.

Evaluation of Disclosure Controls and Procedures. Our management, with the participation of our chief executive officer and 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 chief financial officer concluded that as of the Evaluation Date, our disclosure controls and procedures are effective to ensure that information required to be disclosed by us in the reports that we file or submit under the Exchange Act (i) is recorded, processed, summarized and reported, within the time periods specified in the SEC's rules and forms and (ii) is accumulated and communicated to our management, including our chief executive officer and chief financial officer, as appropriate to allow timely decisions regarding required disclosure.

Changes in Internal Control over Financial Reporting. There were no changes in our internal control over financial reporting that occurred during the period covered by this report that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II
OTHER INFORMATION

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

In August and September 2010, we granted options to purchase an aggregate of 350,000 shares of our common stock at an exercise price of $0.11 per share. These grants were exempt from registration pursuant to Section 4(2) of the Securities Act of 1933, as amended.

On August 6, 2010, a related party note holder converted $40,000 of accrued interest payable into shares of common stock at $.05 per share according to the terms of the note resulting in our issuance of 800,000 shares of our common stock. This transaction was exempt from registration, as it was a nonpublic offering or transaction made pursuant to Section 4(2) of the Securities Act of 1933, as amended. All restricted shares issued in this transaction bore an appropriate restrictive legend.

Item 6. Exhibits.

Exhibit No.	Description
10.31	Promissory Note between Allan M. Robbins and the Company dated August 13, 2010.*

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 pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.*
32.2	Certification of Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.*

* Filed herewith

SIGNATURES

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

	Infinite Group, Inc. (Registrant)
Date: November 10, 2010	/s/ Michael S. Smith Michael S. Smith Chief Executive Officer (Principal Executive Officer)
Date: November 10, 2010	/s/ James Witzel James Witzel Chief Financial Officer (Principal Financial Officer)