

QUANTUM GROUP INC /FL
Form 10QSB
September 19, 2006

**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

FORM 10-QSB

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

FOR THE PERIOD ENDED: July 31, 2006

THE QUANTUM GROUP, INC.

(Exact name of registrant as specified in its charter)

NEVADA	000-31727	20-0774748
(State or other jurisdiction of incorporation or organization)	Commission File Number	(IRS Employer Identification No.)

3420 Fairlane Farms Road, Suite C, Wellington, Florida 33414

(Address, including zip code, of principal executive offices)

(561) 798-9800

(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all documents and reports required to be filed by Sections 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 filings for the past 90 days. YES NO

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

APPLICABLE ONLY TO CORPORATE ISSUERS:

As of August 29, 2006 the number of the Company's shares of par value \$.001 common stock outstanding was 27,064,540.

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PART I FINANCIAL INFORMATION**Item 1.****Financial Statements****THE QUANTUM GROUP, INC.****CONDENSED CONSOLIDATED BALANCE SHEET****AS OF JULY 31, 2006****(A DEVELOPMENT STAGE ENTERPRISE)****(UNAUDITED)****ASSETS****CURRENT ASSETS**

Cash	\$ 16,007
Prepaid interest	112,500
Prepaid other	187,071
Other current assets	2,877
TOTAL CURRENT ASSETS	318,455
PROPERTY AND EQUIPMENT, net of accumulated depreciation of \$64,316	162,880
GOODWILL	23,300

OTHER ASSETS

Software	250,000
Other	17,713
TOTAL ASSETS	\$ 772,348

LIABILITIES AND DEFICIENCY IN ASSETS**CURRENT LIABILITIES**

Accounts payable	\$ 208,630
Accrued liabilities and payroll taxes	410,393
Accrued payroll	1,007,687
Notes payable and accrued interest - shareholder	371,204
Loans payable - current portion	815,780
Other current liabilities	60,000
TOTAL CURRENT LIABILITIES	2,873,694

LONG TERM DEBT

Loans payable	129,641
Capital lease obligation - net of current portion	10,312

TOTAL LONG TERM DEBT	139,953
TOTAL LIABILITIES	3,013,647
COMMITMENTS AND CONTINGENCIES	
DEFICIENCY IN ASSETS ACCUMULATED DURING DEVELOPMENT STAGE	
Common Stock, par value \$.001 per share, 170,000 shares authorized;	25,027
Additional paid in capital	4,365,984
Warrants	44,667
Accumulated deficit	(6,585,581)
Deferred Compensation	(91,396)
TOTAL DEFICIENCY IN ASSETS ACCUMULATED DURING DEVELOPMENT STAGE	(2,241,299)
TOTAL LIABILITIES AND DEFICIENCY IN ASSETS	\$ 772,348

See accompanying notes to condensed consolidated financial statements

THE QUANTUM GROUP, INC.**CONDENSED CONSOLIDATED STATEMENT OF OPERATIONS****(A DEVELOPMENT STAGE ENTERPRISE)****FOR THE NINE MONTHS ENDED JULY 31, 2006 AND 2005**

	For the three month ended		For the nine months ended		For the period
	July 31,		July 31,		July 24, 2001
					(inception)
					to
					July 31,
	2006	2005	2006	2005	2006
Revenues					
Provider network	\$ 13,896	\$	\$ 22,640	\$	\$ 23,759
Provider services	32,782		32,782		32,782
	\$ 46,678	\$	\$ 55,422	\$	\$ 56,541
Direct Costs					
Direct medical costs	\$ 13,896	\$	\$ 22,640	\$	\$ 23,759
Provider services costs	21,752		21,752		21,752
	\$ 35,648	\$	\$ 44,392	\$	\$ 45,511
Gross Profit	\$ 11,030	\$	\$ 11,030	\$	\$ 11,030
General and administrative expenses					
Amortization of deferred financing costs	\$ 934,956	\$	\$ 1,012,508	\$	\$ 1,012,508
Salaries and employee costs	498,982	309,759	1,314,879	843,514	3,318,729
	98,713	39,798	180,971	144,070	637,791

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Consulting expense					
Occupancy	31,609	6,067	65,875	34,670	172,965
Interest	80,501	8,235	118,752	25,785	223,135
Depreciation & amortization	12,965	6,333	34,171	14,694	64,316
Other general & administrative expenses	193,289	94,276	435,318	224,893	1,167,167
Total Expenses	\$ 1,851,015	\$ 464,468	\$ 3,162,474	\$ 1,287,626	\$ 6,596,611
Net expenses representing net loss	\$ (1,839,985)	\$ (464,468)	\$ (3,151,444)	\$ (1,287,626)	\$ (6,585,581)
Basic and diluted (loss) per common share	\$ (0.07)	\$ (0.02)	\$ (0.13)	\$ (0.07)	
Weighted average number of common shares outstanding	24,599,079	21,441,948	23,722,201	19,570,121	

See accompanying notes to condensed consolidated financial statements

THE QUANTUM GROUP, INC.

CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN DEFICIENCY IN ASSETS
ACCUMULATED DURING THE DEVELOPMENT STAGE

JULY 31, 2006

(UNAUDITED)

	Preferred Stock par value \$.001 per share 30,000,000 authorized		Common Stock par value \$.001 per share 170,000,000 authorized		Additional Paid-in Capital		Warrants	Deferred Compensation	Allocated Shares for Deferred Compensation	Accumulated Deficit
	# of Shares	Amount	# of Shares	Amount						
7/03	-	\$-	3,296,885	\$3,297	\$168,351		\$-	\$(531,192)	\$327,150	\$(460,500)
Preferred stock			1,188,122	1,188	276,690					
Accounts payable			300,000	300	164,700					
Retained earnings - stk			197,269	197	172,551		172,748	(172,748)		
Deferred compensation							83,975			
Advance			25,000	25	23,475					
Quantum Inc.	100,000	100	9,300,000	9,300						
Quantum Medical Inc.	100,000	100	4,000,000	4,000						
Stock grants							(45,950)	45,950		
Options					79,800		(79,800)			\$(1,119,900)
7/04	200,000	\$200	18,307,276	\$18,307	\$885,567		\$-	\$(400,219)	\$200,352	\$(1,580,500)
Preferred stock			3,590,128	3,590	1,295,944					
Retained earnings - stk			176,325	176	134,373		232,765	(232,765)		
Deferred compensation			114,000	114	108,716					
Use of cash			317,572	318	179,750					

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Preferred	(200,000)	(200)							
Deferred							91,379		
Purchase			200,000	200	169,800	145,000			
Stock grants							(57,683)	57,683	
Stock					16,350		(16,350)		(1,853,62)
2005	-	\$-	22,705,301	\$22,705	\$2,790,500	\$145,000	\$(150,108)	\$25,270	\$(3,434,13)
Stock			270,000	270	113,930				
Stock - stk			11,300	11	7,819		7,830	(7,830)	
Pension			39,000	39	31,236				
Use of cash									
Deferred							12,267		
Loan			85,000	85	49,915				(602,70)
2006	-	\$-	23,110,601	\$23,110	\$2,993,400	\$145,000	\$(130,011)	\$17,440	\$(4,036,84)
Stock			400,000	400	176,850				
Stock - stk			15,800	16	12,064		12,080	(12,080)	
Pension			1,500	1	2,599				
Warrants						(145,000)			
Deferred							9,500		
Cancellation							13,500	(13,500)	
Stock grants							(108,000)	108,000	
Loan			715,000	715	642,785				(708,75)
2006	-	\$-	24,242,901	\$24,242	\$3,827,698	\$-	\$(202,931)	\$99,860	\$(4,745,55)

ash	183,500	184	165,486		
- stk	11,600	12	9,848	9,860	(9,860)
ensation	30,750	31	26,669		

See accompanying notes to condensed consolidated financial statements

					44,667			
						11,675		
		557,819	558	336,283				(1,839,985)
-	\$-	25,026,570	\$25,027	\$4,365,984	\$44,667	\$(181,396)	\$90,000	\$(6,585,581)

See accompanying notes to condensed consolidated financial statements

THE QUANTUM GROUP, INC.**(A DEVELOPMENT STAGE ENTERPRISE)****CONSOLIDATED STATEMENTS OF CASH FLOWS****FOR THE NINE MONTHS ENDED JULY 31, 2006 AND 2005****(UNAUDITED)**

	Nine months ended		July 24, 2001
	July 31,		(Inception) to
	2006	2005	July 31,
			2006
OPERATING ACTIVITIES			
Net (loss)	\$ (3,151,444)	\$ (1,287,626)	\$ (6,585,582)
Adjustments to reconcile net loss to net cash used in operating activities:			
Depreciation and amortization	34,170	14,694	64,316
Amortization of financing premium	1,012,508	97,067	1,012,508
Amortization of deferred compensation	33,442		347,228
Issuance of stock for compensation	76,015	146,197	362,724
Issuance of stock in lieu of cash	54,000		119,463
Loss on conversion of debt to common stock			135,000
Changes in operating assets and liabilities:			
Decrease (increase) in other assets	58,038	(4,449)	50,890
Increase in accounts payable and accrued liabilities	558,644	308,350	1,604,835
Total adjustments	1,826,817	561,859	3,696,964
Net cash used in operating activities	(1,324,627)	(725,767)	(2,888,618)
INVESTING ACTIVITIES			
Purchase of property and equipment	(38,164)	(122,429)	(158,445)
Purchase of software			(90,000)
Net cash used in investing activities	(38,164)	(122,429)	(248,445)
FINANCING ACTIVITIES			
Proceeds from loans	1,036,000	29,353	1,226,690
Proceeds from issuance of common stock	291,450	985,204	1,953,861

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Repayments on debt	(23,423)	(2,337)	(27,481)
Net cash provided by financing activities	1,304,027	1,012,220	3,153,070
Net increase (decrease) in cash	(58,764)	164,024	16,007
Cash at beginning of period	74,771	35,968	
Cash at end of period	\$ 16,007	\$ 199,992	\$ 16,007
Supplemental disclosures of cash flow information:			
Cash paid during the period for interest	\$ 29,880	\$ 55,175	\$ 72,315
Supplemental disclosures of non-cash investing and financing activities:			
Assumption of Liabilities of Transform Pack International, Inc.	\$	\$	\$ 120,852
Common stock and preferred stock issued in connection with acquisitions	\$	\$	\$ 23,300
Capital lease obligations incurred on purchases of equipment	\$ 19,260	\$	\$ 29,618
Conversion of convertible note into common stock	\$	\$	\$ 30,000
Acquisition of Biocard assets	\$	\$	\$ 315,000
Issuance of stock as deferred finance costs on loans	\$ 1,025,841	\$	\$ 1,025,841
Note payable - fixed asset	\$ 36,953	\$	\$ 36,953

See accompanying notes to condensed consolidated financial statements

THE QUANTUM GROUP, INC.

(A DEVELOPMENT STAGE ENTERPRISE)

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

JULY 31, 2006

(UNAUDITED)

Note 1:

Description of Company

On May 28, 2003, Transform Pack International, Inc. (the Company) merged with Quantum HIPAA Consulting, Inc (Quantum). On January 30, 2004, the shareholders of the Company approved the reincorporation of the Company under the name of The Quantum Group, Inc. (QTUM). The shareholders approved a 1 for 10 reverse stock split. The Company is a development stage company with nominal revenues. The Company's business model is to become a provider of services to the healthcare industry in three complementary areas: providing *healthcare services* to consumers through our provider network; providing *ancillary services* to physicians, such as medical billing and insurance and *developing new technologies* for interconnecting the healthcare delivery system.

Basis of Presentation

The condensed consolidated financial statements of the Company have been prepared in accordance with generally accepted accounting principles for interim financial information and Regulation SB. Accordingly, they do not include all of the information and notes required by generally accepted accounting principles for complete financial statements.

The accompanying condensed consolidated financial statements are unaudited. However, in the opinion of management, they include all adjustments necessary for a fair presentation of financial position, results of operations and cash flows. All adjustments made during the nine months ended July 31, 2006, were of a normal, recurring nature. The amounts presented for the nine months ended July 31, 2006, are not necessarily indicative of the results to be expected for any other interim period or for the entire fiscal year. Additional information is contained in the Annual Report on Form 10-KSB of the Company for the year ended October 31, 2005, which should be read in conjunction with this quarterly report.

Going Concern

The Company has minimal revenues to date. Since its inception, the Company has been dependent upon the receipt of capital investment to fund its continuing activities. In addition to the normal risks associated with a new business venture, there can be no assurance that the Company's business plan will be successfully executed. The Company's ability to execute its business model will depend on its ability to obtain additional financing and achieve a profitable level of operations. There can be no assurance that sufficient financing will be obtained. Nor can any assurance be made that the Company will generate substantial revenues or that the business operations will prove to be profitable. These conditions raise substantial doubt about the Company's ability to continue as a going concern. The financial statements do not include any adjustments that might result from the outcome of these uncertainties.

Note 2:

Summary of Significant Accounting Policies

Cash Equivalents

The Company considers all highly liquid debt instruments with original maturities of three months or less to be cash equivalents. At July 31, 2006, there were no cash equivalents.

Property and Equipment

Furniture and equipment are stated at cost. Depreciation is calculated using the straight-line method over the estimated useful lives of the assets, which range from three to five years.

Research and Development Costs

Research and development costs are charged to expense when incurred.

THE QUANTUM GROUP, INC.

(A DEVELOPMENT STAGE ENTERPRISE)

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

JULY 31, 2006

(UNAUDITED)

Note 2:

Summary of Significant Accounting Policies (Continued)

Use of Estimates

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

Income Taxes

The Company has not recognized any future tax benefit arising from net operating loss carry forwards in the accompanying condensed consolidated financial statements in accordance with the provisions of SFAS No. 109, as the realization of this deferred tax benefit is not likely. A 100% valuation allowance has been established to offset the entire amount of the Company's net deferred tax asset.

Goodwill

On an annual basis, management assesses the composition of the Company's assets and liabilities, as well as the events that have occurred and the circumstances that have changed since the most recent fair value determination. If events occur or circumstances change that would more likely than not reduce the fair value of goodwill below its carrying amount, goodwill will be tested for impairment. The Company will recognize an impairment loss if the carrying value of the asset exceeds the fair value determination. There was no impairment of goodwill as of July 31, 2006.

Principles of Consolidation

The accompanying condensed consolidated financial statements for the period ended July 31, 2006 include the accounts of The Quantum Group, Inc. and its subsidiaries, Renaissance Health Systems, Inc., Quantum Medical Technologies, Inc., QMed Billing, Inc. and The Quantum Agency.

Revenue Recognition

The Company has entered into a full risk contract with a Health Maintenance Organization (HMO). Commencing when the Company has 300 patients, the Company will receive a monthly fee for each patient that chooses one of the Company's physicians as their primary care physician. The fixed fee is based on a percentage of the premium the

HMO receives. Revenue under this agreement is generally recorded in the period services are rendered at the rates then in effect, with quarterly adjustments. The Company started treating patients in September 2005, but has not reached the 300 minimum by July 31, 2006. The Company has recorded income relating to the primary care physician's charges for the nine month period ended July 31, 2006. Medical costs associated with the revenue were equal to the revenue.

In June 2006, the Company entered into a management agreement with a medical billing and collection company. Under the terms of the agreement, the Company paid an amount to the billing and collection company and assumed all management responsibility and financial risk of the operation of the business. The Company has included all the revenues and expenses for this operation in the Company's condensed consolidated financial statements. Revenues are recorded upon the collection of billed service for their clients.

THE QUANTUM GROUP, INC.**(A DEVELOPMENT STAGE ENTERPRISE)****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS****JULY 31, 2006****(UNAUDITED)****Note 2:****Summary of Significant Accounting Policies (Continued)*****Stock Compensation***

The company has adopted Statement of Financial Accounting Standards No. 123 (SFAS 123), Accounting for Stock-Based Compensation. SFAS 123 encourages the use of a fair-value-based method of accounting for stock-based awards, under which the fair value of stock options is determined on the date of grant and expensed over the vesting period. Under SFAS 123, companies may, however, measure compensation costs for those plans using the method prescribed by Accounting Principles Board Opinion No. 25 (APB No. 25), Accounting for Stock Issued to Employees. Companies that apply APB No. 25 are required to include pro forma disclosures of net earnings and earnings per share as if the fair-value-based method of accounting had been applied. The Company elected to account for such plans under the provisions of APB No. 25. The Company accounts for stock options granted to consultants under SFAS 123.

Had the compensation expense for the stock option plan been determined based on the fair value of the options at the grant date consistent with the methodology prescribed under Statement of Financial Standards No. 123, Accounting for Stock Based Compensation, at July 31, 2006, the Company's net loss and loss earnings per share would have been affected to the pro forma amounts indicated below:

	2006	2005
Net loss		
As reported	\$ (3,151,444)	\$ (1,287,626)
Pro forma	\$ (3,376,156)	\$ (1,307,161)
Loss per share		
As reported	\$ (0.13)	\$ (0.07)
Pro forma	\$ (0.14)	\$ (0.08)

The fair value of each option was estimated on the date of grant using the fair market value option-pricing model with the following assumptions:

Risk-free interest rate	3%
Expected life (years)	3
Expected volatility	1.50
Expected dividends	None

New Accounting Pronouncements

In December 2004, the FASB issued SFAS No. 123R *Share-Based Payment* (SFAS 123R), a revision to SFAS No. 123 *Accounting for Stock-Based Compensation* (SFAS 123), and superseding APB Opinion No. 25 *Accounting for Stock Issued to Employees* and its related implementation guidance. SFAS 123R establishes standards for the accounting for transactions in which an entity exchanges its equity instruments for goods or services, including obtaining employee services in share-based payment transactions. SFAS 123R applies to all awards granted after the required effective date and to awards modified, repurchased, or cancelled after that date. Adoption of the provisions of SFAS 123R is effective as of the beginning of the first interim or annual reporting period of the first fiscal year beginning on or after December 15, 2005. The Company believes that the effect of the adoption of SFAS 123R will increase expenses by approximately \$500,000 over a period ending October 31, 2009.

Note 3:**Fair Value of Financial Instruments**

The carrying amounts of cash and cash equivalents, accounts payable, notes payable and accrued liabilities approximate their fair value because of the short maturity of these financial instruments.

THE QUANTUM GROUP, INC.

(A DEVELOPMENT STAGE ENTERPRISE)

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

JULY 31, 2006

(UNAUDITED)

Note 4:

Loss Per Share

Basic loss per share is computed by dividing loss available to common shareholders by the weighted average number of common shares for the period. The computation of diluted loss per share is similar to basic loss per share, except that the denominator is increased to include the number of additional common shares that would have been outstanding if the potentially dilutive common shares, such as options, had been issued. Diluted loss per share is not presented as the effects would be anti-dilutive.

The Company has 626,493 warrants, with exercise prices ranging from \$0.20 to \$0.50 per share, and 1,542,240 with exercise prices ranging from \$0.40 to \$1.50 per share, exercisable at July 31, 2006.

Note 5:

Accrued Liabilities

Accrued liabilities represent expenses that apply to the reported period and have not been billed by the provider or paid by the Company.

Accrued liabilities consisted of the following at July 31, 2006

Accrued Expenses

\$216,903

Delinquent Payroll Taxes and Penalties

104,551

Accrued Interest

65,281

Other

23.658

Note 6:

Incentive Equity and Stock Option Plan

In October 2003 the Company adopted a stock option plan. The purpose of the stock option plan was to increase the employees and non-employee directors proprietary interest in Quantum and to align more closely their interests with the interests of the shareholders of Quantum, as well as to enable Quantum to attract and retain the services of experienced and highly qualified employees and non-employee directors.

Options granted under this plan may either be options qualifying as incentive stock options under Section 422 of the Internal Revenue Code of 1986, as amended, or options that do not so qualify. Any incentive option must provide for an exercise price of not less than 100% of the fair market value of the underlying shares on the date of such grant, but the exercise price of any incentive option granted to an eligible employee owning more than 10% of our common stock must be at least 110% of such fair market value as determined on the date of the grant.

The term of each option and the manner in which it may be exercised is determined by the board of directors, provided that no option may be exercisable more that 10 years after the date of its grant and, in the case of an incentive option granted to an eligible employee owning more that 10% of the our common stock, no more than five years after the date of the grant. The board of directors shall determine the exercise price of non-qualified options.

The Company has reserved 5,000,000 shares of common stock under the plan. The board of directors, or a committee of the board of directors, will administer the plan including, without limitation, the selection of the persons who will be granted plan options under the plan, the type of plan options to be granted, the number of shares subject to each plan options and the plan option price.

The per share exercise price of shares granted under the plan may be adjusted in the event of certain changes in the total purchase price payable upon the exercise in full of options granted under the plan. Officers; directors; and key employees of and consultants to Quantum will be eligible to receive non-qualified options under the plan. Only officers, directors and employees of Quantum who are employed by Quantum, or by any subsidiary thereof, are eligible to receive incentive options.

The Company has elected to account for the stock options under the Accounting Principles Board Opinion No. 25, Accounting for Stock Issued to Employees, and related interpretations. The Company accounts for stock options

granted to consultants under Financial Accounting Standards Board Statement No. 123, Accounting for Stock-Based Compensation.

THE QUANTUM GROUP, INC.**(A DEVELOPMENT STAGE ENTERPRISE)****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS****JULY 31, 2006****(UNAUDITED)****Note 6:****Incentive Equity and Stock Option Plan (continued)**

A summary of options during the nine months ended July 31, 2006 and 2005 is shown below:

	2006			2005		
		Options			Options	
	Incentive Stock Grants	Number of Shares	Weighted Average Exercise Price	IncentiveStock Grants	Number of Shares	Weighted Average Exercise Price
Outstanding at beginning of the period	60,000			60,000		
Granted						
Exercised						
Forfeited						
Outstanding at July 31, Exercisable at July 31,	60,000			60,000		
Available for issuance at July 31 under the plan		4,940,000			4,940,000	

Note 7:**Other Common Stock Transactions**

Deferred Compensation

The Company, from time to time, grants shares of common stock to employees, directors and advisors in lieu of or as partial compensation for services performed for the Company. These shares vest over two and three year periods. The value of the stock is determined by the closing market price at the date of grant. The Company recognized \$47,666 and \$104,787 in compensation expense related to these stock grants for the nine month periods ended July 31, 2006 and 2005. As of July 31, 2006, the Company has 1,542,240 vested options with exercise prices ranging from \$0.40 to \$1.50 per share and expiring in years 2008 through 2011. The Company has granted an additional 971,847 options which have not been vested as of the quarter ended July 31, 2006 with exercise prices ranging from \$0.50 to \$1.50 and expiring in years between 2009 and 2014. These options vest between the years 2006 and 2009.

The Company recorded \$108,000 and \$0 of unearned compensation during the nine month periods ended July 31, 2006 and 2005, respectively, on the grants of stock and recorded the unvested shares as Deferred Compensation - Allocated Shares in the equity section of the balance sheet. The value of the stock is determined by the closing market price on the date of grant and is amortized over a three-month period.

Equity Financing

On July 6, 2005, the Company issued a private placement memorandum to raise \$1,500,000 at a price of \$0.50 per share. The terms include a 13% cash commission plus one common stock warrant at a price of \$0.50 for every \$10.00 raised. The Company realized net proceeds of \$845,031 on the sales of 1,942,600 shares of common stock and issued 99,510 warrants through May 3, 2006. The Company and the placement agent agreed to change the amount of warrants to 10% of shares issued which is consistent with prior agreements with the placement agent and therefore, the Company issued an additional 99,510 warrants.

THE QUANTUM GROUP, INC.

(A DEVELOPMENT STAGE ENTERPRISE)

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

JULY 31, 2006

(UNAUDITED)

Note 7:

Other Common Stock Transactions (continued)

Stock Compensation

From time to time, the Company issues stock to employees as length of service rewards and performance rewards. Additionally, the Company will issue shares to consultants in lieu of cash compensation. These stock issuances are not included in the Company's Incentive Equity and Stock Option Plan. The total shares issued were 101,000 and 188,188 shares for the nine month periods ended July 31, 2006 and 2005, respectively. The value of the stock is determined by the closing market price on the date earned.

Note 8:

Notes Payable

On November 30, 2005, the Company entered into a 13% 2-year callable loan agreement for \$100,000. The terms of the loan agreement include quarterly interest payments and the loan is callable by the lender if any interest payment is not paid within 15 days of being notified by the lender that the interest payment is late. Additional compensation includes 70,000 shares of common stock. The value of the stock was determined by the closing market price on the date of the loan and is amortized over term of the loan. If the Company repays the loan within the first 365 days, the lender will return 17,500 of the shares and if the loan is repaid during the second year, the lender will return 3,000 shares. The Company also paid \$6,500 in commissions to a placement agent.

On May 5, 2006, the Company agreed to a Bridge Financing Agreement with High Capital Funding LLC, the lead lender, for \$501,000. The agreement includes an issuance of an 8% Secured Promissory Note and, as additional consideration, the Company issued 666,667 shares of the Company's common stock. Additional fees include a placement agent fee of \$50,000 plus one 5-year warrant to purchase 66,667 shares of the Company's common stock at a price of \$0.20 per share and a documentation fee of 33,333 shares of the Company's common stock. The common stock issued has registration rights. The value of the stock was determined by the closing market price on the date of the loan and is amortized over term of the loan. The note was to mature upon the earlier of the 80th day following the receipt by the escrow agent of the \$501,000, July 14, 2006, or the second business day following the closing of an aggregate of \$1,000,000 of gross proceeds from a private placement. When the note was not repaid at maturity, the interest rate increased to 18% retroactive to the closing date and the Company issued 33,333 shares, as per the terms of the agreement. On August 21, 2006, the Company and the lead lender agreed to a \$1,000,000 Interim Bridge Financing Agreement whereby the amount owed under the above agreement, \$501,000, was included in the amount

loaned. (See Note 11)

In June 2006, the Company signed six 8% promissory notes for \$25,000 each. The notes were issued pursuant to the May 5, 2006 Bridge Financing Agreement with the lead investor. Each lender was issued 33,333 shares of the Company's common stock. The value of the stock was determined by the closing market price on the date of the loan and is amortized over term of the loan. The terms of the notes were the same as the Bridge Financing Agreement. These notes were not paid at maturity, July 14, 2006, therefore the interest rate was adjusted to 18% retroactively to closing date. On August 21, 2006, the Company and the lead lender agreed to a \$1,000,000 Interim Bridge Financing Agreement whereby the amount owed under the above agreement, the Bridge Financing Agreement, was included in the amount loaned. (See Note 11)

On July 6, 2006, the Company signed an 8% promissory note and financing agreement for \$100,000 with a lender. The terms were consistent with the Bridge Financing Agreement except, among other items, that the note matures the earlier of 80 days from the funding of the note or the second day following the closing of an aggregate of \$2,000,000 of gross proceeds from a private placement. The note is unsecured. The lender and the Company have agreed to extend the loan consistent with the Interim Bridge Financing Agreement dated August 21, 2006. Under this agreement, the lender will be issued 303,030 additional shares. The value of the stock was determined by the closing market price on the date of the loan and is amortized over term of the loan. (See Note 11)

On July 27, 2006, the Company signed a \$60,000 24% demand promissory note with the lead investor. (See Note 11)

THE QUANTUM GROUP, INC.

(A DEVELOPMENT STAGE ENTERPRISE)

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

JULY 31, 2006

(UNAUDITED)

Note 9:

Related Party Transactions

On November 1, 2002, the Company entered into an agreement with a shareholder to purchase certain intellectual property integral to the Company's business. In exchange, the company issued a three (3) year installment note for \$179,080 with an interest rate of eighteen percent (18%) per annum. The price of the sale was equal to the cost the shareholder incurred to develop the property purchased. The note is payable monthly starting January 2003. The Company is in technical default as the Company has not made scheduled payments on the note. The Company is accruing interest at 18% per annum monthly on the unpaid principal balance and has classified the note as current as per the agreement. The principal balance outstanding is \$146,154. The Company paid \$0 and \$55,176 in interest during the nine month period ended July 31, 2006 and 2005, respectively. The interest accrued is \$67,067 and \$39,107 at July 31, 2006 and 2005, respectively.

On November 14, 2005, a shareholder advanced the Company \$50,000. During the quarter ended July 31, 2006, the Company and the shareholder agreed to a 12% interest rate on the unpaid balance and 10,000 shares of common stock. The Company and the lender agreed to extend the loan with terms consistent with the Interim Bridge Financing Agreement dated August 21, 2006 and the Company will issue an additional 151,515 shares of common stock. The value of the stock was determined by the closing market price on the date of the loan and is amortized over term of the loan. (See Note 10)

On December 16, 2005, the Company executed a \$100,000 promissory note payable to Maj-Britt Rosenbaum. This note was due January 31, 2006 and bore an interest rate of 8% per annum payable at term of the note. Additional compensation included 15,000 shares of the Company's common stock per month for each month the debt is outstanding. On February 9, 2006, the husband of the note holder, Michael Rosenbaum, was elected to the Board of Directors of the Company. On February 25, 2006, an additional \$25,000 was advanced to the Company by Mrs. Rosenbaum for a total of \$125,000. Mrs. Rosenbaum and the Company agreed to extend the term of the note based on terms consistent with the Bridge Financing Agreement which includes the issuance of 166,667 shares of common stock. The value of the stock was determined by the closing market price on the date of the loan and is amortized over term of the loan. This loan was not repaid at maturity and is in default converting the interest rate to 18% from May 5, 2006.

Note 10:

Acquisition of Software

On December 16, 2004, Quantum Medical Technologies, Inc. entered into an agreement to purchase application systems provider software from a Florida Limited Liability Corporation for \$80,000. The software was in developmental stage and has received HIPPA certification. The purchase price was to be paid over a period of 120 days from the date of closing. Upon review and testing by an independent software development company, management has determined that certain representations by the seller were not met and therefore the Company has not made any additional payments and will not make further payments on the \$60,000 outstanding balance. The Company is seeking to renegotiate or rescind the purchase with the seller.

THE QUANTUM GROUP, INC.

(A DEVELOPMENT STAGE ENTERPRISE)

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

JULY 31, 2006

(UNAUDITED)

Note 11:

Subsequent Events

In August and September 2006, the Company agreed with the lead lender to execute various 24% promissory notes totaling an additional \$223,000, for a total of \$283,000, which includes the \$60,000 promissory note dated July 27, 2006. These notes were rolled into the \$300,000 credit line included in the Interim Bridge Financing Agreement, dated August 21, 2006.

On August 21, 2006 the Company signed an Interim Bridge Financing Agreement with the lead investor for a maximum of \$1,000,000 to repay the original Bridge Financing Agreement, \$651,000, and raise an additional \$349,000. The agreement provides for an additional \$300,000 credit line. The agreement carries an interest rate of 18% on the first \$651,000, the amount owed on the existing promissory notes above, and 8% on amounts in excess of \$651,000. This agreement matures on the earlier of September 29, 2006 or out of the proceeds from a private placement. As additional compensation and when the Company receives the entire proceeds from the loan, the lenders will receive 3,072,732 shares of the Company's common stock, which includes 909,091 shares for the credit line. Had the 3,072,732 shares been outstanding at July 31, 2006, the loss per share would have been (\$0.07) and (\$0.12) for the three months ended and the nine months ended July 31, 2006.

Item 2.

Management's Discussion and Analysis of Financial Condition and Results of Operations

General

The discussion and analysis set forth below should be read in conjunction with our Condensed Consolidated Financial Statements and the related notes thereto appearing elsewhere in this quarterly report. The information presented for the nine months ended July 31, 2006 and 2005, was derived from unaudited financial statements, which, in our opinion, reflect all adjustments (consisting only of normal recurring adjustments) necessary for a fair presentation.

Forward Looking Statements

This Report on Form 10-QSB contains certain forward-looking statements. When used in this report, press releases and elsewhere by the management of the Company from time to time, the words "believes", "anticipates", and "expects" and similar expressions are intended to identify forward-looking statements that involve certain risks and uncertainties. Additionally, certain statements contained in this discussion may be deemed forward-looking statements that involve a number of risks and uncertainties. Among the factors that could cause actual results to differ materially are the following: the ability of the Company to meet its working capital and liquidity needs, economic trends for consumer advertisers, the availability of long-term credit, unanticipated changes in the U.S. and international economies, business conditions and growth in e-commerce and the timely development and acceptance of new products, the impact of competitive products and pricing, and other risks detailed from time to time in the Company's SEC reports. Readers are cautioned not to place undue reliance on these forward-looking statements, which speak only as of the date hereof. The Company undertakes no obligation to publicly release the results of any events or circumstances after the date hereof or to reflect the occurrence of unanticipated events.

Going Concern

The Company is a development stage company that over the last three years has expensed material sums in developing its provider networks, creating procedures, manuals, infrastructure and systems to support the provider networks and contracting with managed care organizations.

As shown in the accompanying condensed financial statements, the Company has incurred recurring losses and negative cash flows and minimal revenues from its development and organization activities and has negative working capital and shareholders' deficit. Under normal conditions, these conditions raise substantial doubt about the Company's ability to continue as a going concern.

There can be no assurance that the Company will be able to successfully implement its plans to generate additional investor interest and raise additional capital, or if such plans are successfully implemented, that the Company will achieve its goals.

Furthermore, if the Company is unable to raise additional funds, it may be required to modify its growth and developmental plans, or be forced to severely limit development operations or cease operations completely.

The accompanying condensed consolidated financial statements have been prepared assuming that the Company will continue as a going concern and do not include any adjustments to reflect the possible future effects of the recoverability and classification of assets or the amounts and classification of liabilities that might result from the

outcome of this uncertainty. See Liquidity and Capital Resources, below.

Results of Operations

Nine months ended July 31, 2006 and 2005

Revenues for the nine months ended July 31, 2006 were \$55,422 compared to \$0 for the nine month period ended July 31, 2005. The increase is due to the activation of certain HMO contracts and the addition of the management agreement for the billing and collection company. The provider network revenue will remain minimal until the HMO contracts begin full risk.

The expenses for the nine months ended July 31, 2006 were \$3,162,474 compared to \$1,287,626 for the nine month period ended July 31, 2005. The increase of \$1,874,848 was primarily due to an increase of \$1,012,508 in the amortization of deferred financing costs related to the issuance of common stock associated with our financing activities and \$471,365 in personnel related costs which include salaries and the amortization of deferred compensation.

Three months ended July 31, 2006 and 2005

The expenses for the three months ended July 31, 2006 were \$1,851,015 compared to \$464,468 for the three month period ended July 31, 2005. The increase of \$1,386,547 was primarily due to an increase of \$934,956 in the amortization of deferred financing costs related to the issuance of common stock associated with our financing activities and \$189,223 in personnel related costs which include salaries and the amortization of deferred compensation.

Liquidity and Capital Resources

At July 31, 2006, we had working capital deficit of \$2,555,239 as compared to a working capital deficit of \$1,137,194 at July 31, 2005.

Cash inflow from financing activities was \$1,304,027 for the nine months ended July 31, 2006, compared to \$1,012,220 for the nine months ended July 31, 2005. The increase was primarily due to the increase in debt as detailed below. On August 21, 2006, we closed on a \$1,000,000 Interim Bridge Financing Agreement, which includes an additional \$300,000 line of credit. We also had \$104,551 in delinquent payroll taxes at July 31, 2006 and \$113,308 currently remain delinquent. We intend to borrow money from the Interim Bridge Agreement funds to pay the delinquent taxes .

On May 5, 2006, we agreed to a Bridge Financing Agreement with High Capital Funding LLC, the lead lender, for \$501,000. The agreement includes an issuance of an 8% Secured Promissory Note and as additional consideration we issued 666,667 shares of the Company's common stock. Additional fees include a placement agent fee of \$50,000 plus one 5-year warrant to purchase 66,667 shares of the Company's common stock at a price of \$0.20 per share and a documentation fee of 33,333 shares of the Company's common stock. The common stock issued has registration rights. The note was to mature upon the earlier of the 80th day following the receipt by the escrow agent of the \$501,000, July 14, 2006, or the second business day following the closing of an aggregate of \$1,000,000 of gross proceeds from a private placement. When the note was not repaid at maturity, the interest rate increased to 18% retroactive to the closing date and we issued 33,333 shares, as per the terms of the agreement. On August 21, 2006, the Company and the lead lender agreed to a \$1,000,000 Interim Bridge Financing Agreement whereby the amount owed under the above agreement, \$501,000, was included in the amount loaned. In June 2006, we signed six 8% promissory notes for \$25,000 each. The notes were issued pursuant to Bridge Financing Agreement with the lead investor. Each lender was issued 33,333 shares of the Company's common stock. These notes were not paid at maturity, July 14, 2006, therefore the interest rate was adjusted to 18% retroactively to the closing date. On August 21, 2006, we signed an Interim Bridge Financing Agreement with the lead investor for a maximum of \$1,000,000 to repay the original Bridge Financing Agreement, \$651,000, and raise an additional \$349,000. The agreement also provides for an additional \$300,000 credit line. The agreement carries an interest rate of 18% on the first \$651,000, the amount owed on the existing promissory notes above, and 8% on amounts in excess of \$651,000. This agreement matures on September

29, 2006 or out of the proceeds from a private placement. As additional compensation, the lenders receive 3,072,732 shares of the Company's common stock, which include 909,091 shares for the credit line. Between the period July 27, 2006 and August 30, 2006, the Company and the lead lender executed various 24% promissory notes totaling \$283,000. These notes were rolled into the \$300,000 credit line included in the Interim Bridge Financing Agreement.

On July 6, 2006, we signed an 8% promissory note and financing agreement for \$100,000 with a lender. The terms were consistent with the Bridge Financing Agreement except that the note matures the earlier of 80 days from the funding of the note or out of the proceeds from a private placement. . The note is unsecured. The lender and the Company have agreed to extend the loan consistent with the Interim Bridge Financing Agreement dated August 21, 2006. Under this agreement, the lender will be issued 303,030 additional shares.

We have executed agreements with three managed care organizations (MCO), covering 3 counties in Florida. We have started to recognize a minimal amount of revenue through the third quarter ended July 31, 2006 from one of the contracts. Revenue from this contract will significantly increase when we go to full risk, which will occur when the managed care organization reaches 300 members in the 3 counties which we have contracted. We will start generating revenue from the remaining two contracts upon regulatory approval of the managed care organizations plans in the counties in which we will provide health care. We are continually negotiating with other MCOs in order to expand its service area and increase revenue. Additionally, we have secured Errors and Omission insurance policy to protect it from any potential suits related to its responsibility for the managed care organization.

Our development plan includes the identification, negotiation with and acquisition or joint venturing of businesses and services that will allow us to provide comprehensive provider network services including medical management systems, billing and collection and other complementary services that will allow the small to medium size medical organization to provide better care, better medical outcomes and earn more profit. We expect to acquire or joint venture with candidate businesses after extensive due diligence. If the candidate business is to be acquired we expect to secure financing for the acquisition by selling common and/or preferred shares, issuing debt or notes and by leveraging the potential acquisition.

We require additional capital, in the short term, in order to continue our operations, and payoff the Interim Bridge Financing and \$275,000 in short term debt. Additionally, there is no assurance that we will be able to execute on our plans and, clearly, to continue our operations and to implement our current business plan, we will require significant additional long term financing.

New Accounting Pronouncements

In December 2004, the FASB issued SFAS No. 123R Share-Based Payment (SFAS 123R), a revision to SFAS No. 123 Accounting for Stock-Based Compensation (SFAS 123), and superseding APB Opinion No. 25 Accounting for Stock Issued to Employees and its related implementation guidance. SFAS 123R establishes standards for the accounting for transactions in which an entity exchanges its equity instruments for goods or services, including obtaining employee services in share-based payment transactions. SFAS 123R applies to all awards granted after the required effective date and to awards modified, repurchased, or cancelled after that date. Adoption of the provisions of SFAS 123R is effective as of the beginning of the first interim or annual reporting period of the first fiscal year beginning after December 15, 2005. We believe that the effect of the adoption of SFAS 123R will increase expenses approximately \$500,000 over a period ending October 31, 2009.

Item 3.

Controls and Procedures

Our Management and resources are limited. As of July 31, 2006 we had only twenty-eight full time employees, of which three are also officers and directors of the Company. These positions are President/CEO, CFO and Vice President of Administration. Collectively, these officers have conducted an evaluation of the effectiveness of our disclosure controls and procedures (as defined in Rule 13a-15(e) and 15d-15(e) promulgated under the Securities and Exchange Act of 1934, as amended) as of the end of the fiscal quarter covered by this report. Based upon that evaluation, and both our limited developmental history as well as the size of our organization, our management has concluded that we have adequate disclosure controls. However, we must improve procedures for effective and timely gathering, analyzing and disclosing the information we are required to disclose in our reports filed under the Securities

Exchange Act of 1934, as amended. Management expects to add additional controls and personnel in the near future as capital becomes available. There have been no significant changes made in our internal controls or in other factors that could significantly affect our internal controls during the fiscal quarter covered by this report.

PART II OTHER INFORMATION

Item 1.

Legal Proceedings

The Company is not a party to any litigation.

Item 2.

Unregistered Sales of Equity Securities and Use of Proceeds

On December 16, 2005, we executed a \$100,000 promissory note payable to Maj-Britt Rosenbaum. This note was due January 31, 2006 and bears an interest rate of 8% per annum payable at term of the note. Additional compensation includes 15,000 shares of the Company's common stock per month for each month the debt is outstanding. On February 9, 2006, the husband of the note holder, Michael Rosenbaum, was elected to the Board of Directors of the Company. On February 25, 2006, an additional \$25,000 was advanced to us by Mrs. Rosenbaum for a total of \$125,000. Mrs. Rosenbaum and the Company agreed to extend the term of the note based on terms consistent with the Bridge Financing Agreement which includes the issuance of 166,667 shares of common stock. This loan was not repaid at maturity and is in default converting the interest rate to 18% from May 5, 2006

On May 5, 2006, the Company agreed to a Bridge Financing Agreement with High Capital Funding LLC, the lead lender, for \$501,000. The agreement included an issuance of an 8% Secured Promissory Note and, as additional consideration, the Company is to issue 666,667 shares of the Company's common stock. Additional fees include a placement agent fee of \$50,000 plus one 5-year warrant to purchase 66,667 shares of the Company's common stock at a price of \$0.20 per share and a documentation fee of 33,333 shares of the Company's common stock. The common stock issued has registration rights.. The note was to mature upon the earlier of 80th day following the receipt by the escrow agent of the \$501,000, July 14, 2006, or the second business day following the closing of an aggregate of \$1,000,000 of gross proceeds from a private placement. When the note was not repaid at maturity, the interest rate increased to 18% retroactive to the closing date and the Company issued 33,333 shares, as per the terms of the agreement. On August 21, 2006, the Company and the lead lender agreed to a \$1,000,000 Interim Bridge Financing Agreement whereby the amount owed under the above agreement, \$501,000, was included in the amount loaned. The shares were issued as restricted shares under the 1933 Act and were endorsed with a restrictive legend.

In June 2006, the Company signed six 8% promissory notes for \$25,000 each. The notes were issued pursuant to Bridge Financing Agreement with the lead investor. Each lender was issued 33,333 shares of the Company's common stock. The terms of the notes were the same as the Bridge Financing Agreement. The shares were issued as restricted shares under the 1933 Act and were endorsed with a restrictive legend.

On July 6, 2006, the Company signed an 8% promissory note and financing agreement for \$100,000 with a lender. The terms were consistent with the Bridge Financing Agreement except that the note matures the earlier of 80 days from the funding of the note or the second day following the closing of an aggregate of \$2,000,000 of gross proceeds from a private placement. The note is unsecured. The lender and the Company have agreed to extend the loan

consistent with the Interim Bridge Financing agreement dated August 21, 2006. Under this agreement, the lender will be issued 303,030 additional shares. The shares were issued as restricted shares under the 1933 Act and were endorsed with a restrictive legend.

Item 3.

Defaults Upon Senior Securities

The \$501,000 Bridge Financing Agreement dated May 5, 2006 and the six 8% promissory notes totaling \$150,000, originated in June 2006, were due July 14, 2006 and are in default. The lead lender and the Company signed an Interim Bridge Financing Agreement, dated on August 21, 2006, for a maximum of \$1,000,000 to repay the original Bridge Financing Agreement, \$651,000.

Additionally, the Rosenbaum note for \$125,000 carried the same terms as the Bridge Financing Agreement dated May 5, 2006 and was in default and the Company has been contacted by an attorney representing Rosenbaum.

Item 4.

Submission of Matters to a Vote of Security-Holders

On August 31, 2006, the Company held an annual shareholder meeting. Of the 24,979,209 shares outstanding on July 21, 2006, 13,489,605 shares voted. The shareholders voted 13,428,567 for, 0 against and 50,000 abstentions to reelect the current Board to serve until the shareholder meeting in 2007; 13,475,598 for, 0 against and 2,969 abstentions to appoint the public accounting firm of Daszkal, Bolton, LLP as its independent auditors for the year ending October 31, 2006; and 13,340,798 for, 134,800 against and 2,969 abstentions to effectuate a reverse stock split of the Company's common stock at a future date to be determined by the Board of Directors of the Company.

Item 5.

Other Information

None

Item 6.

Exhibits

Exhibits: Copies of the following documents are included or furnished as exhibits to this report pursuant to Item 601 of Regulation S-B.

Exhibit	SEC Ref.	Title of Document
No.	No.	
31.1	31	Certification of the Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
31.2	31	Certification of the Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
32.1	32	Certification of the Chief Executive Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
32.2	32	Certification of the Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

Reports on Form 8-K: None

SIGNATURE

In accordance with the requirements of the Securities Exchange Act of 1934, the Registrant has caused this report to be signed on its behalf by the undersigned, duly authorized.

Date: September 19, 2006

THE QUANTUM GROUP, INC.

BY: /s/ NOEL J. GUILLAMA
Noel J. Guillama, President