

POSITRON CORP  
Form 10QSB  
August 21, 2006

FORM 10-QSB

JUNE 30, 2006

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

**FORM 10-QSB**

- x QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934 FOR THE QUARTERLY PERIOD ENDED JUNE 30, 2006.
- .. TRANSITION REPORT UNDER SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934 FOR THE TRANSITION PERIOD FROM \_\_\_\_\_ TO \_\_\_\_\_.

Commission file number: 000-24092

Positron Corporation

(Exact name of small business issuer as specified in its charter)

Texas  
(State of incorporation)

76-0083622  
(IRS Employer Identification No.)

1304 Langham Creek Drive, Suite 300, Houston, Texas 77084  
(Address of principal executive offices)

(281) 492-7100  
(Issuer's telephone number)

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

Indicate by check mark whether the issuer (1) filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the past 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      ..

As of August 14, 2006, there were 81,135,202 shares of the Registrant's Common Stock, \$.01 par value outstanding.

Transitional Small Business Disclosure Format (check one). Yes \_\_\_\_\_ No \_\_\_ x



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**PART 1 - FINANCIAL INFORMATION****ITEM 1. Financial Statements****POSITRON CORPORATION****BALANCE SHEETS**

(In thousands, except share data)

	<b>June 30, 2006</b> (Unaudited)	<b>December 31,</b> <b>2005</b>
<b><u>ASSETS</u></b>		
Current assets:		
Cash and cash equivalents	\$ 248	\$ 209
Accounts receivable	65	--
Inventories	198	202
Prepaid expenses	--	66
Other receivables	22	--
Receivable from affiliated entities	168	--
Other current assets	69	21
<b>Total current assets</b>	<b>770</b>	<b>498</b>
Investment in joint ventures	750	230
Property and equipment, net	96	120
Deferred loan costs	215	--
Other assets	104	57
<b>Total assets</b>	<b>\$ 1,935</b>	<b>\$ 905</b>
<b><u>LIABILITIES AND STOCKHOLDERS' EQUITY</u></b>		
Current liabilities:		
Accounts payable, trade and accrued liabilities	\$ 1,673	\$ 1,694
Customer deposits	15	15
Unearned revenue	157	66
Deposits for Unissued Series G Preferred Stock	--	195
Convertible notes payable to affiliated entity, less discount of \$514 and \$890	1,619	627
<b>Total current liabilities</b>	<b>3,464</b>	<b>2,597</b>
Convertible notes payable to affiliated entity	800	1,216
Convertible notes payable, less discount of \$1,270	30	--
Derivative liabilities for convertible debentures	2,268	--

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Total liabilities	6,562	3,813
Stockholders' equity (deficit):		
Series A Preferred Stock: \$1.00 par value; 8% cumulative, convertible, redeemable; 5,450,000 shares authorized; 464,319 shares issued and outstanding	464	464
Series C Preferred Stock: \$1.00 par value; 6% cumulative, convertible, redeemable; 840,000 shares authorized; 770,000 shares issued and outstanding	770	770
Series G Preferred Stock: \$1.00 par value; 8% cumulative, convertible, redeemable; 3,000,000 shares authorized; 204,482 shares issued and outstanding	1,096	--
Common Stock: \$0.01 par value; 800,000,000 shares authorized; 80,335,202 shares issued and 76,385,202 shares outstanding	803	778
Additional paid-in capital	58,765	57,364
Subscription receivable	--	(30)
Accumulated deficit	(66,510)	(62,239)
Treasury Stock: 60,156 common shares at cost	(15)	(15)
Total stockholders' equity (deficit)	(4,627)	(2,908)
Total liabilities and stockholders' equity	\$ 1,935	\$ 905

See accompanying notes

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**POSITRON CORPORATION**  
**STATEMENTS OF OPERATIONS**

(In thousands, except per share data)  
(Unaudited)

	Three Months Ended		Six Months Ended	
	June 30, 2006	June 30, 2005	June 30, 2006	June 30, 2005
<b>Revenues:</b>				
System sales	\$ --	\$ --	\$ --	\$ --
Upgrades	--	34	--	34
Service and component	266	171	464	350
<b>Total revenues</b>	<b>266</b>	<b>205</b>	<b>464</b>	<b>384</b>
<b>Costs of revenues:</b>				
System sales	--	87	--	176
Upgrades	--	8	--	8
Service, warranty and component	180	75	328	126
<b>Total costs of revenues</b>	<b>180</b>	<b>170</b>	<b>328</b>	<b>310</b>
<b>Gross profit</b>	<b>86</b>	<b>35</b>	<b>136</b>	<b>74</b>
<b>Operating expenses:</b>				
Research and development	116	104	260	260
Selling and marketing	375	213	445	443
General and administrative	470	392	906	708
Stock based compensation	(25)	3	221	(102)
<b>Total operating expenses</b>	<b>936</b>	<b>712</b>	<b>1,832</b>	<b>1,309</b>
<b>Loss from operations</b>	<b>(850)</b>	<b>(677)</b>	<b>(1,696)</b>	<b>(1,235)</b>
<b>Other income (expense)</b>				
Interest Income	--	1	--	1
Interest expense	(301)	(273)	(570)	(353)
Derivative losses	(1,887)	--	(1,887)	--
Equity in losses of joint ventures	(77)	--	(118)	--
<b>Total other income (expense)</b>	<b>(2265)</b>	<b>(272)</b>	<b>(2,575)</b>	<b>(352)</b>
<b>Net loss</b>	<b>\$ (3,115)</b>	<b>\$ (949)</b>	<b>\$ (4,271)</b>	<b>\$ (1,587)</b>
<b>Basic and diluted loss per common share</b>	<b>\$ (0.04)</b>	<b>\$ (0.02)</b>	<b>\$ (0.05)</b>	<b>\$ (0.03)</b>

Weighted average number of basic and diluted common shares outstanding	79,896	53,303	78,995	53,286
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See accompanying notes

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**POSITRON CORPORATION**  
**STATEMENTS OF CASH FLOWS**

(In thousands)  
(Unaudited)

	Six Months Ended	
	June 30, 2006	June 30, 2005
Cash flows from operating activities:		
Net loss	\$ (4,271)	\$ (1,587)
Adjustment to reconcile net loss to net cash used in operating activities		
Depreciation	24	42
Amortization of loan costs, debt discount and beneficial conversion features	423	233
Stock based compensation	220	(102)
Loss on derivative liabilities	1,887	--
Common stock issued for services	292	--
Equity in losses of joint ventures	118	--
Changes in operating assets and liabilities:		
Accounts receivable	(65)	--
Inventory	3	(63)
Prepaid expenses	66	(14)
Other current assets	(104)	18
Field service parts and supplies	(9)	(3)
Accounts payable and accrued liabilities	3	83
Customer deposits	--	1
Unearned revenue	92	(11)
Net cash used in operating activities	(1,321)	(1,403)
Cash flows from investing activities:		
Capital expenditures	--	(12)
Investment in joint venture	(639)	--
Advance to affiliated company	(132)	--
Purchase of software license	(50)	--
Net cash used in investing activities	(821)	(12)
Cash flows from financing activities:		
Proceeds from notes payable to an affiliated entity	200	1,650
Net proceeds from issuance of convertible debentures	1,080	--
Net proceeds from issuance Series G Preferred Stock	901	--
Net cash provided by financing activities	2,181	1,650



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Net increase in cash and cash equivalents		39		235
Cash and cash equivalents, beginning of period		209		133
Cash and cash equivalents, end of period	\$	248	\$	368
Supplemental cash flow information:				
Interest paid	\$	--	\$	--
Income taxes paid		--		--
Non-cash disclosures				
Issuance of common stock to satisfy severance obligation	\$	25	\$	--
Convertible debenture discount with corresponding increase to paid in capital for value of warranty	\$	919	\$	--
Convertible debenture discount with corresponding increase to derivative liabilities for beneficial conversion feature	\$	2,268	\$	--

See accompanying notes

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**POSITRON CORPORATION**  
**SELECTED NOTES TO FINANCIAL STATEMENTS****1. Basis of Presentation**

The accompanying unaudited interim financial statements have been prepared in accordance with generally accepted accounting principles and the rules of the U.S. Securities and Exchange Commission, and should be read in conjunction with the audited financial statements and notes thereto contained in the Annual Report on Form 10-KSB for Positron Corporation (the "Company") for the year ended December 31, 2005. In the opinion of management, all adjustments, consisting of normal recurring adjustments, necessary for a fair presentation of financial position, results of operations and cash flows for the interim periods presented have been reflected herein. The results of operations for interim periods are not necessarily indicative of the results to be expected for the full year. Notes to the financial statements which would substantially duplicate the disclosures contained in the audited financial statements for the most recent fiscal year ended December 31, 2005, as reported in the Form 10-KSB, have been omitted.

**2. Accounting Policies****Revenue Recognition**

Revenues from POSICAM™ system contracts are recognized when all significant costs have been incurred and the system has been shipped to the customer. Revenues from maintenance contracts are recognized over the term of the contract. Service revenues are recognized upon performance of the services.

**Stock-Based Compensation**

Effective January 1, 2006 the Company adopted the revision to SFAS 123 ("SFAS 123R"), "Share-Based Payment", that focuses primarily on accounting for transactions in which an entity obtains employee services in share-based payment transactions utilizing the modified prospective method. This statement replaces SFAS 123, "Accounting for Stock-Based Compensation", and supersedes APB Opinion No. 25, "Accounting for Stock Issued to Employees". SFAS 123R requires companies to expense the fair value of employee stock options and similar awards.

**3. Going Concern**

Since its inception, the Company has been unable to sell POSICAM™ systems in quantities sufficient to be operationally profitable. Consequently, the Company has sustained substantial losses. At June 30, 2006, the Company had an accumulated deficit of \$66,510,000 and a stockholders' deficit of \$4,627,000. Due to the sizable prices of the Company's systems and the limited number of systems sold or placed in service each year, the Company's revenues have fluctuated significantly from year to year.

The Company utilized net proceeds of \$1,096,000 from the issuance of Series G Preferred Stock and \$1,080,000 in net proceeds from subordinated notes payable to fund its operating activities for the six month period ended June 30, 2006. As a result, the Company had cash and cash equivalents of \$248,000 at June 30, 2006. At the same date, the Company had accounts payable and accrued liabilities of \$1,673,000. In addition, debt service and working capital requirements for the upcoming year may reach beyond current cash balances. The Company plans to continue to raise funds as required through equity and debt financings to sustain business operations. These factors raise substantial

doubt about the Company's ability to continue as a going concern.

There can be no assurance that the Company will be successful in implementing its business plan and ultimately achieving operational profitability. The Company's long-term viability as a going concern is dependent on its ability to 1) achieve adequate profitability and cash flows from operations to sustain its operations, 2) control costs and expand revenues from existing or new business and 3) meet current commitments and fund the continuation of its business operation in the near future.

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4. Inventories

Inventories at June 30, 2006 and December 31, 2005 consisted of the following (in thousands):

	June 30, 2006	Dec. 31, 2005
Raw materials	\$ 211	\$ 235
Work in process	37	17
Subtotal	248	252
Less reserve for obsolescence	(50)	(50)
Total	\$ 198	\$ 202

5. Investment in Joint VenturesNeusoft Positron Medical Systems Co. Ltd.

The Company has entered into a joint venture with a Chinese company for the production of its PET scanners. On June 30, 2005 the Company entered into a Joint Venture Contract with Neusoft Medical Systems Co., Inc. of Shenyang, Lianoning Province, People's Republic of China ("Neusoft"). Pursuant to the Joint Venture Contract the parties formed a jointly-owned company, Neusoft Positron Medical Systems Co., Ltd. (the "JV Company"), to engage in the manufacturing of PET and CT/PET medical imaging equipment. The JV Company received its business license and was organized in September 2005.

The Company and Neusoft are active in researching, developing, manufacturing, marketing and/or selling Positron Emission Tomography ("PET") technology and both parties seek to mutually benefit from each other's strengths, and intend to cooperate in the research, development and manufacturing of PET technology. The purpose and scope of the JV Company's technology business is to research, develop and manufacture Positron Emission Tomography systems (PET), and an integrated X-ray Computed Tomography system (CT) and PET system (PET/CT), and to otherwise provide relevant technical consultation and services.

The parties to the joint venture contributed an aggregate of US \$2,000,000 in capital contributions. Neusoft contributed US\$ 1,350,000 to the JV Company for the issuance of 67.5% of the JV Company's capitalization. The Company contributed US\$ 650,000 to the JV Company, of which US\$ 250,000 was made in cash, and US\$ 400,000 was made in the form of a technology license for the issuance of 32.5% of the JV Company's capitalization. The Company has transferred to the JV Company certain of its PET technology, while Neusoft made available to the JV Company certain CT technology for the development and production of an integrated PET/CT system. The parties will share the profits, losses and risks of the JV Company in proportion to and, in the event of losses, to the extent of their respective contributions to the registered capital of the JV Company.

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## CONDENSED FINANCIAL STATEMENTS FOR THE JV COMPANY

**NEUSOFT POSITRON MEDICAL SYSTEMS CO., LTD.  
CONDENSED BALANCE SHEET****June 30, 2006**

(in thousands)

ASSETS

## Current assets:

Cash and cash equivalents	\$	578
Other current assets		459
Total current assets		1,037

Intangibles and other assets		653
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Total assets	\$	1,690
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CAPITAL

Capital		1,690
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Total capital	\$	1,690
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**NEUSOFT POSITRON MEDICAL SYSTEMS CO., LTD.  
CONDENSED STATEMENT OF OPERATIONS****SIX MONTH PERIOD ENDED JUNE 30, 2006**

(in thousands)

Revenue	\$	--
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## Expense

General and administrative expense		270
Total expense		270

Net loss	\$	(270)
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**Imaging PET Technologies Inc.**

The Company and Quantum Molecular Pharmaceuticals Inc., a Canadian radiopharmaceutical corporation (“Quantum”) acquired all of the operating assets of IS2 Medical Systems Inc., a developer and manufacturer of nuclear imaging devices based in Ottawa, Ontario, Canada (“IS2”) through a minority-owned subsidiary of the Company, Imaging PET Technologies, Inc. (“IPT”). The Company and Quantum hold 49.9% and 50.1%, respectively, of the total registered

capital of IPT. On May 8, 2006, to finalize certain obligations of Quantum related to the Quantum Molecular Technologies Joint Venture, the Company agreed to issue Series B Convertible Preferred Stock (the "Series B"), convertible into 65,000,000 shares of the Company's common stock, to IPT in exchange for a promissory note in the amount of \$1,300,000. See, *Quantum Molecular Technologies Joint Venture*, below.

On June 5, 2006, IPT completed the acquisition of IS2. Pursuant to an assumption agreement with IS2 and assignment agreements with IS2's secured debt holders, IPT acquired all of IS2's operating assets and assumed certain of its liabilities.

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## CONDENSED FINANCIAL STATEMENTS FOR IPT

**IMAGING PET TECHNOLOGIES, INC.  
CONDENSED BALANCE SHEET****June 30, 2006**

(in thousands)

ASSETS

## Current assets:

Cash and cash equivalents	\$	261
Inventories		1,472
Other current assets		673
<b>Total current assets</b>		<b>2,406</b>

Fixed and other assets		168
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<b>Total assets</b>	<b>\$</b>	<b>2,574</b>
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LIABILITIES AND CAPITAL

## Current liabilities:

Accounts payable and other current liabilities	\$	1,367
<b>Total current liabilities</b>		<b>1,367</b>

Non-current liabilities		4
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<b>Total liabilities</b>		<b>1,371</b>
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Capital		1,203
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<b>Total liabilities and capital</b>	<b>\$</b>	<b>2,574</b>
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**IMAGING PET TECHNOLOGIES, INC.  
CONDENSED STATEMENT OF OPERATIONS  
PERIOD FROM JUNE 4 (DATE OF ACQUISITION) TO JUNE 30, 2006  
(in thousands)**

Revenue	\$	600
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Cost of goods sold		473
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Gross profit		127
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Expense	
Operating expenses	179
Other expenses	9
Net loss	\$ (61)

### **Quantum Molecular Technologies Joint Venture**

On May 8, 2006, the Company amended certain aspects of the Quantum Molecular Technologies Joint Venture (“QMT”) formed with Quantum Molecular Pharmaceuticals, Inc. and IMAGIN Diagnostic Centres, Inc. on December 28, 2005. QMT is developing certain next generation technologies including PET-enabled surgical tools and solid-state photo detector technology, which have implications in both molecular imaging and PET and could have further application in the military and aerospace segments. The first solid-state detector technology patent application has been filed by QMT.

Whereas the Company originally held 20% of the interests of QMT, Quantum and IMAGIN assigned 100% of their interests in QMT to the Company. Additionally, the investment amount Quantum and IMAGIN originally committed to in the amount of \$4,000,000 was restated to \$2,400,000 to reflect the assignment of the QMT interests and participation by the Company in the IPT joint venture and subsequent financing. The investment will be in the form of installment payments, the first of which is due on October 1, 2006. In exchange for the assignment of QMT interests and the investments, the Company will issue Series B Convertible Preferred Stock, convertible into 345,000,000 shares of the Company’s common stock to Quantum and IMAGIN, pro rata. The installment payments are secured by the pledge of the Series B, which have not yet been issued by the Company



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6. **Other Assets**

Other assets at June 30, 2006 and December 31, 2005 consisted of the following (in thousands):

	June 30, 2006	Dec. 31, 2005
Field service parts and supplies	\$ 54	\$ 45
Deferred loan costs	--	12
Software license	50	--
Total	\$ 104	\$ 57

7. **Accounts Payable and Accrued Liabilities**

Accounts payable and accrued liabilities at June 30, 2006 and December 31, 2005 consisted of the following (in thousands):

	June 30, 2006	Dec. 31, 2005
Trade accounts payable	\$ 376	\$ 441
Accrued royalties	356	352
Sales taxes payable	238	236
Accrued interest	312	260
Accrued compensation	125	159
Accrued property taxes	117	113
Accrued professional fees	50	80
Other accrued liabilities	99	53
Total	\$ 1,673	\$ 1,694

Accrued compensation includes severance payments payable to the Company's former Chief Executive Officer, Gary H. Brooks. Mr. Brooks resigned effective September 29, 2005. In connection with his resignation, the Company agreed to make severance payments to Mr. Brooks of \$18,583.33 per month for a period of six months, and to extend the expiration date of options held by Mr. Brooks through September 30, 2006, and warrants held by Mr. Brooks until the later of (i) October 31, 2007 for 7,000,000 warrants and June 2009 for 500,000 warrants, and (ii) the date on which a registration statement filed with the Securities Exchange Commission permitting a sale of the shares underlying such warrants shall have become effective and shall have remained effective for a period of six months. The Company owed approximately \$55,000 on this severance obligation at June 30, 2006.

8. **Convertible Notes Payable to Affiliated Entities**

Notes payable to affiliated entities at June 30, 2006 and December 31, 2005 consisted of the following (in thousands):

	June 30, 2006	Dec. 31, 2005
IMAGIN Diagnostic Centres, Inc., less discount of \$354 and \$604	\$ 1,545	\$ 1,096
Positron Acquisition Corp., less discount of \$0 and 6	634	627
Solaris Opportunity Fund, L.P., less discount of \$160 and \$280	240	120
Total	\$ 2,419	\$ 1,843



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In January 2006, the Company received the final \$100,000 installment of funds from the October 31, 2005 sale of \$400,000 worth of 10% convertible promissory notes to IMAGIN Diagnostic Centres, Inc.

On March 17, 2006, IMAGIN Diagnostic Centres, Inc. assigned to Positron Acquisition Corp. its interest in 770,000 shares of the Company's Series C Preferred Stock, 4,026,000 shares of the Company's common stock and the Company's secured convertible notes in the aggregate principal amount of \$696,850, which are convertible into 696,850 shares of the Company's Series D Preferred Stock and in turn are convertible into 27,874,000 shares of the Company's common stock.

9. **Stockholders' Equity**

The Company's former Chief Executive Officer, Gary H. Brooks, exercised options for the purchase of 500,000 shares of common stock in the first quarter of 2006. The exercise of these options resulted in an increase in stockholders' equity and a decrease in the severance obligation (Note 7) by \$25,000.

The Company cancelled subscriptions receivable totaling \$30,000 that were due from a former Director and a former Chief Executive Officer. Cancellation of the subscriptions receivable reduced additional paid-in capital.

At the Annual Meeting of Shareholders held May 18, 2006, the shareholders of the Company approved an amendment and restatement to the Articles of Incorporation to increase the number of authorized shares of Common Stock to 800,000,000.

10. **Series G Preferred Stock**

During the three months ended June 30, 2006, the Company issued 204,482 Units in a private placement. Each Unit consists of one share of a new series of preferred stock designated Series G Preferred Stock and a warrant exercisable for 50 shares of common stock (the "Units"). The purchase price was \$5.50 per Unit, with \$5.00 of the Unit purchase price allocated to the purchase of the share of Series G Preferred Stock and \$0.50 allocated to the purchase of the warrant, for a total offering amount of \$1,124,650. The net proceeds of the private placement were approximately \$1,096,000.

Each share of Series G Preferred Stock is convertible into 100 shares of common stock. Eight percent dividends accrue on the Series G Preferred Stock and may be paid in cash or in Common Stock in the Company's discretion. The Series G Preferred Stock is senior to the Company's common stock and junior in priority to the Registrant's Series A, C, D, E and F Preferred Stock in liquidation. Except as required by law and in the case of various actions affecting the rights of the Series G Preferred Stock, holders of the Series G Preferred Stock are not entitled to vote on matters requiring shareholder vote. While the Series G Preferred Stock is outstanding or any dividends thereon remain unpaid, no common stock dividends may be paid or declared by the Company. The Series G Preferred Stock may be redeemed in whole or in part, at the option of the Company, at any time at a price of \$5.00 per share plus any undeclared and/or unpaid dividends to the date of redemption.

11. **Secured Convertible Notes Payable**

Pursuant to the terms of a Security Agreement and a Registration Rights Agreement (the "Agreements") dated May 23, 2006, the Company agreed to issue to private investors (the "Investors") callable secured convertible notes (the

“Debentures”) in the amount of \$2,000,000, with interest at the rate of 6% annually. The Debentures are convertible into shares of the Company’s Common Stock at the product of the “Applicable Percentage” and the average of the lowest three (3) trading prices for the common stock during the twenty (20) day period prior to conversion. Applicable Percentage is 50%; provided, however that the percentage shall be increased to (i) 55% in the event that a Registration Statement is filed within thirty days of the closing of the transaction and (ii) 65% in the event the Registration Statement becomes effective within one hundred and twenty days of the closing of the transaction. The notes also contain antidilutive provisions for pricing. The Company filed a Registration Statement on June 20, 2006. The Company may repay principal and interest in cash in the event that the price of the Company’s Common Stock is below \$0.20 on the last business day of a month (at amounts ranging from 120% to 140% based on the timing). Pursuant to the terms of the Agreements, the Company issued to the Investors warrants to purchase 30,000,000 shares of Common Stock at an exercise price of \$0.15 per share. These warrants are exercisable seven (7) years from the closing of the transaction.

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On May 23, 2006 the Company issued Debentures in the amount of \$700,000 with a maturity date of May 23, 2009. On June 21, 2006 the Company issued Debentures in the amount of \$600,000 with a maturity date of June 21, 2009. Pursuant to the terms of the Agreements, the Company shall issue Debentures and receive the third tranch in the amount of \$700,000 when the Registration Statement is declared effective by the Securities and Exchange Commission. Legal and other fees incurred in conjunction with the Debentures issued on May 23, 2006 and June 21, 2006 were \$130,000 and \$90,000, respectively and are being amortized over the maturity periods of the Debentures.

As a result of the beneficial conversion features contained in the Convertible Debentures, the derivatives embedded in the Debentures have been classified as derivative liabilities. Fair value of the embedded derivatives is determined using the Black Sholes Valuation Method. The combined liabilities recorded during the three and six months ended June 30, 2006 totaled \$2,268,000. Of such amount, \$380,600 was recorded as debt discount and is being amortized over the term of the Debentures and \$1,887,000 was immediately charged to loss on derivative obligations during the three months ended June 30, 2006. Additionally, the Company recorded a discount of \$919,400 against the Convertible Debentures for the fair market value of the warrants issued. The discount, which was recorded as an increase to stockholders' equity, is being amortized to interest expense over the term of the Debentures, utilizing the effective interest method.

12. **Loss Per Share**

Basic loss per common share is based on the weighted average number of common shares outstanding in each period and earnings adjusted for preferred stock dividend requirements. Diluted earnings per common share assume that any dilutive convertible preferred shares outstanding at the beginning of each period were converted at those dates, with related interest, preferred stock dividend requirements and outstanding common shares adjusted accordingly. It also assumes that outstanding common shares were increased by shares issuable upon exercise of those stock options and warrants for which market price exceeds exercise price, less shares which could have been purchased by the Company with related proceeds. The convertible preferred stock and outstanding stock options and warrants were not included in the computation of diluted earnings per common share for the three and six month periods ended June 30, 2006 and 2005 since it would have resulted in an antidilutive effect.

The following table sets forth the computation of basic and diluted earnings per share.

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	Three Months Ended		Six Months Ended	
	June 30, 2006	June 30, 2005	June 30, 2006	June 30, 2005
(In Thousands, except per share data)				
Numerator				
Basic and diluted loss	\$ (3,115)	\$ (949)	\$ (4,271)	\$ (1,587)
Denominator				
Basic and diluted earnings per share- weighted average shares outstanding	79,896	53,303	78,995	53,286
Basic and diluted loss per common share	\$ (0.04)	\$ (0.02)	\$ (0.05)	\$ (0.03)

13. **Litigation**

From time to time the Company may be involved in various legal actions in the normal course of business for which the Company maintains insurance. The Company is currently not aware of any material litigation affecting the Company.

14. **Stock Based Compensation**

In connection with the May 2004 transaction with IMAGIN, the Company re-priced various options and warrants to employees that are subject to the variable accounting rules. The market price of the Company's common stock increased from \$0.09 at December 31, 2005 to \$0.12 at June 30, 2006. Due to the increase in price, application of the variable accounting rules resulted in stock based compensation of \$116,000 during the six months ended June 30, 2006. The market price of the Company's common stock decreased \$0.03 from \$0.12 at December 31, 2004 to \$0.09 at June 30, 2005. Due to the decline in price, application of the variable accounting rules resulted in the reversal of stock based compensation by \$102,000 during the six month period ended June 30, 2005. For the three months ended June 30, 2006 and 2005, the Company recognized a reversal of stock based compensation of \$25,000 and stock based compensation expense of \$3,000, respectively.

Effective January 1, 2006 the Company adopted the revision to SFAS 123 ("SFAS 123R"), "Share-Based Payment", that focuses primarily on accounting for transactions in which an entity obtains employee services in share-based payment transactions utilizing the modified prospective method. This statement replaces SFAS 123, "Accounting for Stock-Based Compensation", and supersedes APB Opinion No. 25, "Accounting for Stock Issued to Employees". SFAS 123R requires companies to expense the fair value of employee stock options and similar awards. The Company estimates the amount of stock-based compensation expense related to currently outstanding options to be approximately \$51,000 and \$105,000 for the three and six months ended June 30, 2006, respectively.

The expected life of the options is determined using a simplified method, computed as the average of the option vesting periods and the contractual term of the option. For performance based options that vest upon the occurrence of an event, the Company uses an estimate of when the event will occur as the vesting period used in the Black-Scholes calculation for each option grant.

Based on the Company's previous two years' forfeitures, the Company has adjusted the calculated value of the options

for the three and six months ended June 30, 2006 using a 32.1% average estimated forfeiture rate.

14.

**Stock Based Incentive Plan**

On April 10, 2006, the Company's Board of Directors adopted a 2006 Stock Incentive Plan ("2006 Plan"). The 2006 Plan is administered by the Board and provides for the direct issuance of stock and grants of nonqualified stock options to directors, officers, employees and consultants. The administrator is authorized to determine the terms of each award granted under the plan, including the number of shares, exercise price, term and exercisability. Stock and options may be granted for services rendered or to be rendered. A total of 5,000,000 shares of common stock have been authorized for issuance under the 2006 Plan. On April 10, 2006, 2,000,000 shares of common stock were issued to a consultant under the 2006 Plan. Accordingly the Company recorded consulting expense equal to the fair market value of the shares issued of \$292,000.

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

We are including the following cautionary statement in this Quarterly Report on Form 10-QSB to make applicable and utilize the safe harbor provision of the Private Securities Litigation Reform Act of 1995 regarding any forward-looking statements made by, or on behalf of, the Company. Forward-looking statements include statements concerning plans, objectives, goals, strategies, future events or performance and underlying assumptions and other statements, which are other than statements of historical facts. Certain statements contained herein are forward-looking statements and, accordingly, involve risks and uncertainties, which could cause actual results or outcomes to differ materially from those expressed in the forward-looking statements.

Our expectations, beliefs and projections are expressed in good faith and are believed by us to have a reasonable basis, including without limitations, our examination of historical operating trends, data contained in our records and other data available from third parties, but there can be no assurance that our expectations, beliefs or projections will result, or be achieved, or be accomplished.

**Comparison of the Results of Operations for the Three Months ended June 30, 2006 and 2005**

We experienced a loss of \$3,115,000 for the three months ended June 30, 2006 compared to a loss of \$949,000 for the same quarter in 2005. The significant increase in the loss is due primarily to \$1,887,000 of derivatives losses resulting from the fair market valuation of embedded derivatives in convertible debentures issued during the period.

Although the Company earned no revenue from system upgrades during the three months ended June 30, 2006, revenue earned under service contract was \$266,000 which accounted for all revenues during the period. Total revenues for the three month period ended June 30, 2005 were \$205,000 of which \$171,000 came from service contracts and \$34,000 from system upgrades. The increase in service revenue is attributable to several customers executing service contracts after the expiration of the warranty received with the original purchase of their PET systems.

The Company generated gross profits of \$86,000 during the three months ended June 30, 2006 compared to gross profits of \$35,000 for the same three months in 2005. Costs of sales and services for the three months ended June 30, 2005 included \$87,000 related to system sales; there were no costs of system revenues for the same period in 2006. Cost of revenues associated with service contracts were \$180,000 and \$75,000 for the three month periods ending June 30, 2006 and 2005, respectively.

Operating expenses increased \$224,000 to \$936,000 for the three months ended June 30, 2006 from \$712,000 for the same period in 2005. Sales and marketing expense for the three months ended June 30, 2006 increased to \$375,000 from \$213,000 for the same period in 2005. This significant increase resulted primarily from \$292,000 of consulting fees which were exchanged for shares of the Company's common stock. Sales and marketing salaries for the second quarter of 2006 were \$16,000 compared to \$122,000 during the second quarter of 2005. General and administrative expenses increased \$78,000 to \$470,000 in the quarter ended June 30, 2006 from \$392,000 in the same period in 2005. This increase in general and administrative expenses primarily resulted from increased consulting fees expensed in 2006. Net stock based compensation of \$(25,000) for the quarter ended June 30, 2006 is due to the reversal of previously recorded compensation associated with re-priced options resulting from a decrease in the price of the Company's common stock.





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Interest expense of \$301,000 in the second quarter of 2005 compared to \$273,000 of interest expense in the same period in 2005. During the three months ended June 30, 2006 equity in losses of joint ventures was \$77,000. The Company's investments in the joint ventures were made subsequent to the quarter ended June 30, 2005 and therefore no equity adjustments were recorded during the second quarter 2005.

**Comparison of the Results of Operations for the Six Months ended June 30, 2006 and 2005**

The company had net losses of \$4,271,000 and \$1,587,000 for the six months ended June 30, 2006 and June 30, 2005, respectively. The increase in the loss in 2006 resulted primarily from derivative losses. Increases in interest expense, stock based compensation, and equity in losses of joint venture investments also contributed to the increased loss in 2006.

No revenues were generated from sales of systems during the six months ended June 30, 2006 or the six months ended June 30, 2005. Revenues of \$464,000 for the six months ended June 30, 2006 consisted exclusively of revenue from service contracts and components, as compared to \$350,000 of service revenue for the same period in 2005 while total revenues for the 2005 period were \$384,000. Increased service revenue is attributed to new service contract with customers whose warranties on their PET systems expired.

Gross profit for the six months ended June 30, 2006 was \$136,000 or 29.3% compared to \$74,000 or 19.2% for the same period in 2005. Improved gross profit is attributable in large part to decreases in cost of revenues expenses including a decrease in salaries and related expenses of nearly \$50,000.

Operating expenses increased \$523,000 to \$1,832,000 for the six months ended June 30, 2006 from \$1,309,000 for the same period in 2005. Research and development expenses were consistent at \$260,000 for each of the six month periods. Sales and marketing expense for the six months ended June 30, 2006 was \$445,000 compared to \$443,000 for the same period in 2005. The increase in general and administrative expenses primarily resulted from increased consulting fees for certain outsourced services and projects. Overall general and administrative increased to \$906,000 from \$708,000 for the six months ended June 30, 2006 and 2005, respectively. The company recorded stock based compensation of \$221,000 for the six months ended June 30, 2006. A reversal of stock based compensation of \$102,000 relating to the application of the variable accounting rules to the re-pricing of warrants and options was recorded in the first six months of 2005.

Interest expense of \$570,000 for the six months ended June 30, 2006 is an increase of \$217,000 over interest expense of \$353,000 for the six months ended June 30, 2005. The Company issued \$1,500,000 of new convertible secured debentures during the six months ended June 30, 2006. Interest expense in the first six months of 2006 includes \$414,700 in amortization of loan costs, debt discounts and beneficial conversion features. For the six months ended June 30, 2006 the Company recorded equity in the losses of joint ventures of \$118,000.

**Financial Condition**

The Company had cash and cash equivalents of \$248,000 on June 30, 2006. On the same date, accounts payable and accrued liabilities outstanding totaled \$1,673,000. The Company did not sell any imaging systems in the six-month period ended June 30, 2006. Sales of imaging systems and/or additional debt or equity financings will eventually be necessary to resolve the Company's liquidity issues and allow it to continue to operate as a going concern. However, there is no assurance that the Company will be successful in selling new systems or securing additional debt or equity

financing.

Since inception, we have been unable to sell our POSICAM™ systems in quantities sufficient to be operationally profitable. Consequently, we have sustained substantial losses. Due to the sizable selling prices of our systems and the limited number of systems sold or placed into service each year, revenues have fluctuated significantly from year to year. We have an accumulated deficit of \$66,510,000 at June 30, 2006. The Company will need to increase system sales to achieve profitability in the future.

These events raise doubt as to our ability to continue as a going concern. The report of our independent public accountants, which accompanied our financial statements for the year ended December 31, 2005, was qualified with respect to that risk. If we are unable to obtain debt or equity financing to meet our cash needs we may have to severely limit or cease our business activities or may seek protection from our creditors under the bankruptcy laws.

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**New Accounting Pronouncements**

In February 2006, the Financial Accounting Standards Board (“FASB”) issued Financial Accounting Standard (“FAS”) No. 155, “Accounting for Certain Hybrid Financial Instruments, an amendment of FAS No. 133 and 140.” FAS No. 155 resolves issues addressed in FAS No. 133 Implementation Issue No. D1, “Application of Statement 133 to Beneficial Interests in Securitized Financial Assets,” and permits fair value remeasurement for any hybrid financial instrument that contains an embedded derivative that otherwise would require bifurcation, clarifies which interest-only strips and principal-only strips are not subject to the requirements of FAS No. 133, establishes a requirement to evaluate interests in securitized financial assets to identify interests that are freestanding derivatives or that are hybrid financial instruments that contain an embedded derivative requiring bifurcation, clarifies that concentrations of credit risk in the form of subordination are not embedded derivatives and amends FAS No. 140 to eliminate the prohibition on a qualifying special-purpose entity from holding a derivative financial instrument that pertains to a beneficial interest other than another derivative financial instrument. FAS No. 155 is effective for all financial instruments acquired or issued after the beginning of the first fiscal year that begins after September 15, 2006. The Company is currently evaluating the effect of the adoption of FAS No. 155 but believes it will not have a material impact on its financial position or results of operations.

In March 2006, the FASB issued FAS No. 156, “Accounting for Servicing of Financial Assets, an amendment of FAS No. 140.” FAS No. 156 requires an entity to recognize a servicing asset or liability each time it undertakes an obligation to service a financial asset by entering into a servicing contract under a transfer of the servicer’s financial assets that meets the requirements for sale accounting, a transfer of the servicer’s financial assets to a qualified special-purpose entity in a guaranteed mortgage securitization in which the transferor retains all of the resulting securities and classifies them as either available-for-sale or trading securities in accordance with FAS No. 115, “Accounting for Certain Investments in Debt and Equity Securities” and an acquisition or assumption of an obligation to service a financial asset that does not relate to financial assets of the servicer or its consolidated affiliates. Additionally, FAS No. 156 requires all separately recognized servicing assets and servicing liabilities to be initially measured at fair value, permits an entity to choose either the use of an amortization or fair value method for subsequent measurements, permits at initial adoption a one-time reclassification of available-for-sale securities to trading securities by entities with recognized servicing rights and requires separate presentation of servicing assets and liabilities subsequently measured at fair value and additional disclosures for all separately recognized servicing assets and liabilities. FAS No. 156 is effective for transactions entered into after the beginning of the first fiscal year that begins after September 15, 2006. The Company is currently evaluating the effect of the adoption of FAS No. 156 but believes it will not have a material impact on its financial position or results of operations.

**Critical Accounting Policies****Revenue Recognition**

Revenues from POSICAM™ system contracts are recognized when all significant costs have been incurred and the system has been shipped to the customer. Revenues from maintenance contracts are recognized over the term of the contract. Service revenues are recognized upon performance of the services.

**Stock-Based Compensation**

Effective January 1, 2006 the Company adopted the revision to SFAS 123 (“SFAS 123R”), “Share-Based Payment”, that

focuses primarily on accounting for transactions in which an entity obtains employee services in share-based payment transactions utilizing the modified prospective method. This statement replaces SFAS 123, "Accounting for Stock-Based Compensation", and supersedes APB Opinion No. 25, "Accounting for Stock Issued to Employees". SFAS 123R requires companies to expense the fair value of employee stock options and similar awards.

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**ITEM 3 - CONTROLS AND PROCEDURES**

As of June 30, 2006, the Company carried out an evaluation, under the supervision and with the participation of the Company's management, including the Company's Chairman of the Board and Chief Financial Officer of the effectiveness of the design and operation of the Company's disclosure controls and procedures (as defined in Exchange Act Rule 13a-15(e) and Rule 15d-15(e)). Based upon that evaluation, the Company's Chairman of the Board and Chief Financial Officer concluded that the Company's disclosure controls and procedures are effective at a reasonable level. There has been no change in the Company's internal control over financial reporting that occurred during the Company's most recent fiscal quarter that has materially affected or is reasonably likely to materially affect, the Company's internal control over financial reporting.

The Company's management, including the Chairman of the Board and Chief Financial Officer, do not expect that the Company's disclosure controls or internal control over financial reporting will prevent all error and all fraud. A control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met due to numerous factors, ranging from errors to conscious acts of an individual, or individuals acting together. In addition, the design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. Because of the inherent limitations in a cost-effective control system, misstatements due to error and/or fraud may occur and not be detected.

**PART II OTHER INFORMATION****ITEM 1 - LEGAL PROCEEDINGS**

From time to time the Company may be involved in various legal actions in the normal course of business for which the Company maintains insurance. The Company is currently not aware of any material litigation affecting the Company.

**ITEM 2 - UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS**

None

**ITEM 3 - DEFAULTS UPON SENIOR SECURITIES**

None

**ITEM 4 - SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS**

At the Company's annual meeting of shareholders held on May 18, 2006, a majority of the Company's shareholders approved an amendment and restatement to the Company's Articles of Incorporation to increase the number of shares of authorized common stock, par value \$.01 per share, from 100,000,000 shares to 800,000,000.

**ITEM 5 - OTHER INFORMATION**

On May 31, 2006, Solaris Opportunity Fund, L.P., a Delaware limited partnership ("Solaris") transferred all of its

interest in the Company's Convertible Notes and Series F Convertible Notes to Quantum Molecular Pharmaceuticals, Inc., a Canadian corporation ("QMP") and wholly-owned subsidiary of Imagin Diagnostic Centres, Inc., a Canadian corporation ("IDC"). As reported in Solaris' Form 4 filed on June 5, 2006, and subsequent amendments thereto, the Convertible Notes are in the aggregate principal amount of \$740,000 and convertible into 37,000,000 shares of the Registrant's common stock and the Series F Convertible Note is in the principal amount of \$400,000 and convertible into 20,000,000 shares of the Company's common stock. Solaris received a promissory note in the principal amount of \$11,400,000 and options to purchase 50,000,000 shares of the Company's common stock at an exercise price of \$.05 per share. Prior to this sale, IDC held rights to 87,749,000 shares of the Company's common stock. Patrick G. Rooney, the Company's Chairman of the Board, is the managing director of Solaris' managing partner.

**ITEM 6 - EXHIBITS**

- (a) Exhibits
- 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.

(b) Reports on Form 8-K. During the second quarter of 2006 and to the date of the filing of this quarterly report, the Company filed four Form 8-K Current Reports on May 26, 2006, June 1, 2006, June 2, 2006 and July 14, 2006. The reports disclosed a Regulation FD disclosure, the Company's financing with private investors in the amount of \$2,000,000, the resignation of the Company's registered accounting firm and the retention of the Company's new registered accounting firm, respectively.

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**SIGNATURES**

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

POSITRON CORPORATION  
(Registrant)

Date: August 18, 2006      /s/ Patrick G. Rooney  
Patrick G. Rooney  
Chairman of the Board

Date: August 18, 2006      /s/ Corey N. Conn  
Corey N. Conn  
Chief Financial Officer

**EXHIBIT INDEX**

Exhibit	Description of the Exhibit
<u>31.1</u>	Chairman of the Board Certification of Periodic Financial Report Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.*
<u>31.2</u>	Chief Financial Officer Certification of Periodic Financial Report Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.*
<u>32.1</u>	Chairman of the Board Certification Pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.#
<u>32.2</u>	Chief Financial Officer Certification Pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes Oxley Act of 2002.#

\* Filed herewith

# Furnished herewith

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