

SIPEX CORP
Form 10-Q
May 13, 2003

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SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended March 29, 2003
or

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

For the transition period from to

Commission file number: 0-27892

SIPEX Corporation

(Exact Name of Registrant as Specified in its Charter)

Massachusetts
(State or Other Jurisdiction of
Incorporation or Organization)

04-6135748
(I.R.S. Employer
Identification No.)

(408) 934-7500

Registrant's telephone number, including area code

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

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Act). Yes No

There were 28,030,659 shares of the Registrant's Common Stock issued and outstanding as of May 9, 2003.

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SIPEX CORPORATION
CONDENSED CONSOLIDATED BALANCE SHEETS
(In thousands, except per share data)
(Unaudited)

	March 29, 2003	December 31, 2002
(in thousands, except per share data)		
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 9,736	\$ 6,489
Short-term investment securities	2,001	9,980
Accounts receivable, less allowances of \$900 and \$945 at March 29, 2003 and December 31, 2002, respectively	10,581	7,278
Inventories	12,056	14,393
Prepaid expenses and other current assets	2,258	3,446
	36,632	41,586
Total current assets	36,632	41,586
Property, plant, and equipment, net	55,632	56,997
Other assets	221	203
	92,485	98,786
Total assets	\$ 92,485	\$ 98,786
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	\$ 7,517	\$ 8,103
Accrued expenses	4,323	3,570
Accrued restructuring costs	532	755
Deferred income	2,281	1,383
	14,653	13,811
Total current liabilities	14,653	13,811
Long-term debt	10,531	10,455
	25,184	24,266
Total liabilities	25,184	24,266
Shareholders' equity:		
Preferred stock, \$0.01 par value, 1,000 shares authorized and no shares issued or outstanding		
Common stock, \$0.01 par value, 40,000 shares authorized and 28,031 shares issued and outstanding	280	280
Additional paid-in capital	175,489	175,489
Accumulated deficit	(108,401)	(101,179)
Accumulated other comprehensive loss	(67)	(70)
	67,301	74,520
Total shareholders' equity	67,301	74,520
Total liabilities and shareholders' equity	\$ 92,485	\$ 98,786

See accompanying notes to condensed consolidated financial statements

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CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(In thousands, except per share data)
(Unaudited)

	Three Months Ended	
	March 29, 2003	March 30, 2002
Net sales	\$ 15,117	\$ 16,063
Cost of sales	15,097	13,888
Gross profit	20	2,175
Operating expenses:		
Research and development	2,933	2,714
Marketing and selling	1,924	2,266
General and administrative	1,969	1,655
Restructuring and facility exit costs	(6)	
Total operating expenses	6,820	6,635
Loss from operations	(6,800)	(4,460)
Other expense, net	(241)	(387)
Loss before income taxes	(7,041)	(4,847)
Income tax expense (benefit)	181	(1,890)
Net loss	\$ (7,222)	\$ (2,957)
Net loss per common share basic and diluted	\$ (0.26)	\$ (0.12)
Weighted average common and common equivalent shares outstanding basic and diluted	28,031	24,874

See accompanying notes to condensed consolidated financial statements

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	Three Months Ended	
	March 29, 2003	March 30, 2002
Operating activities:		
Net loss	\$(7,222)	\$(2,957)
Adjustments to reconcile net loss to net cash used in operating activities:		
Increase in deferred income taxes		(1,897)
Provision for uncollectable receivables and returns and allowances	259	307
Depreciation	1,808	2,128
Provision for inventories	630	500
Amortization of discount on long-term debt	76	
Amortization of discount on short-term investment securities	(21)	
Changes in current assets and liabilities:		
(Increase) decrease in accounts receivable	(3,562)	959
Decrease (increase) in inventories	1,707	(2,040)
Decrease (increase) in prepaid expenses and other current assets	1,188	(72)
Increase in other assets	(18)	
(Decrease) increase in accounts payable	(586)	1,833
Increase in accrued expenses	753	948
Decrease in accrued restructuring costs	(223)	
Increase (decrease) in deferred income	898	(351)
Net cash used in operating activities	<u>(4,313)</u>	<u>(642)</u>
Investing activities:		
Proceeds from maturity of short-term investment securities	8,000	
Purchase of property, plant and equipment	(443)	(443)
Net cash provided by (used in) investing activities	<u>7,557</u>	<u>(443)</u>
Financing activities:		
Proceeds from issuance of common stock		379
Payments of debt obligations		(1,421)
Net cash used in financing activities		<u>(1,042)</u>
Effect of foreign currency translation adjustments	3	(22)
Increase (decrease) in cash and cash equivalents	3,247	(2,149)
Cash and cash equivalents, beginning of period	6,489	4,874
Cash and cash equivalents, end of period	<u>\$ 9,736</u>	<u>\$ 2,725</u>
Supplemental cash flow information:		
Cash paid during the period for:		
Income taxes	\$	\$ 1

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Interest	\$ 180	\$ 68
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See accompanying notes to condensed consolidated financial statements

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SIPEX CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

Note 1 Basis of Presentation

Unaudited Interim Financial Information

We have prepared the accompanying condensed consolidated financial statements pursuant to the rules and regulations of the Securities and Exchange Commission (the SEC) for interim financial reporting. As used herein, Sipex, the Company, we, our and similar terms include Sipex Corporation and its wholly-owned subsidiaries, unless the context indicates otherwise. These condensed consolidated financial statements are unaudited and, in our opinion, include all adjustments, consisting of normal recurring adjustments and accruals necessary for a fair presentation of the consolidated balance sheets, operating results and cash flows for the periods presented. Operating results for the three months ended March 29, 2003 are not necessarily indicative of the results that may be expected for the year ending December 31, 2003 due to cyclical and other factors. Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States have been omitted in accordance with the rules and regulations of the SEC. These condensed consolidated financial statements should be read in conjunction with the audited consolidated financial statements and accompanying notes included in our Annual Report on Form 10-K for the year ended December 31, 2002. Certain prior period amounts have been reclassified to conform to the current period presentation.

Principles of Consolidation

The consolidated financial statements include the accounts of Sipex and all of its wholly owned subsidiaries. All intercompany accounts and transactions have been eliminated in consolidation.

Note 2 Effect of Recent Accounting Pronouncements

In April 2002, the FASB issued SFAS No. 145, *Rescission of FASB Statement Nos. 4, 44, and 64, Amendment of FASB Statement No. 13 and Technical Corrections*, effective for fiscal years beginning May 15, 2002 or later. It rescinds SFAS No. 4, *Reporting Gains and Losses From Extinguishments of Debt*, SFAS No. 64, *Extinguishments of Debt to Satisfy Sinking-Fund Requirements*, and SFAS No. 44, *Accounting for Intangible Assets of Motor Carriers*. This Statement also amends SFAS No. 13, *Accounting for Leases*, to eliminate an inconsistency between the required accounting for sale-leaseback transactions and the required accounting for certain lease modifications that have economic effects similar to sale-leaseback transactions. This Statement also amends other existing authoritative pronouncements to make various technical corrections, clarify meanings or describe their applicability under changed conditions. On January 1, 2003, the Company adopted SFAS No. 145 with no material impact on its financial position, results of operations or cash flows.

In June 2002, the FASB issued SFAS No. 146, *Accounting for Costs Associated With Exit or Disposal Activities*. SFAS No. 146 requires companies to recognize costs associated with exit or disposal activities when they are incurred rather than at the date of commitment to an exit or disposal plan. This Statement is effective for exit or disposal activities initiated after December 31, 2002. On January 1, 2003, the Company adopted SFAS No. 146 and there was no material impact on its financial position or results of operations. Management does not expect that SFAS 146 will have a significant impact to the Company's financial position, results of operations or cash flows.

In November 2002, the FASB issued FASB Interpretation No. 45, *Guarantors Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others* (FIN 45). FIN 45 requires that upon issuance of a guarantee, a guarantor must recognize a liability for the fair value of a stand-ready to perform obligation assumed under a guarantee. Additionally, a guarantor must recognize a contingent obligation to make future payments when such obligation becomes probable and estimable. FIN 45 also requires additional disclosures by a guarantor in its interim and annual financial statements about the obligations associated with guarantees issued. The recognition provisions of FIN 45 will be effective for any guarantees that are issued or

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modified after December 31, 2002. The Company does not guarantee any obligations. The adoption of this interpretation did not have a material impact on the Company's financial statements.

Note 3 Stock-Based Compensation

In December 2002, the FASB issued SFAS No. 148, *Accounting for Stock-Based Compensation - Transition and Disclosure - an Amendment of SFAS 123*. SFAS No. 148 provides additional transition guidance for those entities that elect to voluntarily adopt the provisions of SFAS No. 123, *Accounting for Stock-Based Compensation*. Furthermore, SFAS No. 148 mandates prominent disclosures in both interim and year-end financial statements about the fair value based method of accounting for stock-based employee compensation and the effect of the method used on reported results. SFAS No. 148 is effective for fiscal years ending after December 15, 2002. The adoption of SFAS No. 148 did not have a material effect on the Company's financial position or results of operations as the Company does not intend to adopt the fair value method of accounting for stock-based employee compensation.

The Company accounts for its stock-based employee compensation plans under the recognition and measurement principles of APB Opinion No. 25, *Accounting for Stock Issued to Employees*, and related interpretations. No stock based compensation cost is reflected in net loss, as all options granted under those plans had an exercise price equal to the market value of the underlying common stock on the date of grant. The following table illustrates the effect on net loss and net loss per share as if the Company had applied the fair value recognition provisions of FASB Statement No. 123, *Accounting for Stock Based Compensation*, as amended by SFAS No. 148, to stock-based employee compensation in each period.

	3 Months Ended	3 Months Ended
	March 29, 2003	March 30, 2002
Net loss	\$ (7,222)	\$ (2,957)
Add: Total stock-based employee compensation expense determined under fair value based method for all awards, net of related tax effects	(4,304)	(2,429)
Pro forma net loss	(11,526)	(5,386)
Net loss per share:		
Basic and diluted as reported	(0.26)	(0.12)
Basic and diluted proforma	(0.41)	(0.22)

The fair value for each award granted was estimated at the date of grant using the Black-Scholes option-pricing model, assuming no expected dividends and the following weighted average assumptions:

	3 Months Ended	3 Months Ended
	March 29, 2003	March 30, 2002
Average risk-free interest rates	3.0%	4.0%
Average expected life (in years)	6.0	6.0
Volatility	171%	247%

Note 4 Net Loss Per Share

Basic net loss per share is based upon the weighted average number of common shares outstanding. Diluted net loss per share is based upon the weighted average number of common and common equivalent shares outstanding assuming dilution. Common equivalent shares, consisting of outstanding stock options and warrants, are included in the per share calculations where the effect of their inclusion would be dilutive. As the Company is in a net loss position, the weighted average number of common and common equivalent shares outstanding equals the weighted average number of common and common equivalent shares assuming dilution. Antidilutive potential common shares excluded from the dilution calculation represent 7,368,000 and 4,926,000 potential common shares for March 29, 2003 and March 30, 2002, respectively.

Note 5 Valuation and Qualifying Accounts

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The Company had the following activity for the sales returns, bad debt and inventory reserves (in thousands):

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	<u>Sales Returns</u>	<u>Bad Debt</u>	<u>Total A/R Allowances</u>	<u>Inventory</u>
Balance December 31, 2002	\$ 653	\$ 292	\$ 945	\$4,865
Charged to costs and expenses	270	(11)	259	630
Usage of reserves	(304)		(304)	(995)
	<u> </u>	<u> </u>	<u> </u>	<u> </u>
Balance at March 29, 2003	\$ 619	\$ 281	\$ 900	\$4,500
	<u> </u>	<u> </u>	<u> </u>	<u> </u>

Note 6 Restructuring

Below is a summary of the activity related to restructuring costs for the first quarter of 2003.

	<u>Restructuring Costs</u>
Accrual balance 12/31/02	\$ 755
Incurred 2003	
Charges utilized	(217)
Adjustments to accrual	(6)
	<u> </u>
Accrual balance 03/29/03	\$ 532
	<u> </u>

During the first quarter of 2003, the Company paid \$217,000 on the accrued restructuring balance of \$755,000 outstanding as of December 31, 2002. The payments consisted mainly of employee severance costs. In addition, the accrual was reduced by \$6,000 for the reversal of accrued facility exit costs. The balance of the accrual as of March 29, 2003 consists of severance costs which are expected to be paid during the second quarter of 2003.

Note 7 Contingencies

In February 1999, Sipex filed a lawsuit against Maxim Integrated Products, Inc. (Maxim) with the U.S. District Court for the District of Massachusetts seeking a declaratory judgment that three of Sipex's products did not infringe Maxim patents. Maxim filed counterclaims alleging certain products sold by Sipex infringe a Maxim patent. The counterclaims seek injunctive relief and unspecified damages. Sipex has denied infringement and alleges that the patent is invalid. The Company expects to settle this lawsuit in the near future within the amounts accrued in the accompanying condensed consolidated financial statements.

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

Forward-Looking Statements

From time to time, information provided by us, statements made by our employees or information included in our filings with the Securities and Exchange Commission (including in this Form 10-Q) may contain statements which are not historical facts, known as forward-looking statements, and are made pursuant to the safe harbor provision of the Private Securities Litigation Reform Act of 1995. In particular, certain statements contained in the Management's Discussion and Analysis of Financial Condition and Results of Operations and Factors Affecting Future Results Sections below which are not historical facts (including, but not limited to, statements concerning anticipated availability of capital for working capital and for capital expenditures, potential litigation settlements, and statements regarding revenue recognition policies, including estimates of future returns) constitute forward-looking statements. Any such statements are not promises or guarantees but are subject to risks and uncertainties that may cause our actual future results to differ materially from those stated in any forward-looking statements. Factors that may cause such differences include, but are not limited to, the factors discussed below and the other risks discussed in our other filings with the Securities and Exchange Commission. The following discussion should be read in conjunction with the financial statements and notes to the financial statements included in this Form 10-Q, as well as the Management Discussion and Analysis of Financial Condition and Results of Operations contained in our most recent Form 10-K. We caution you not to place undue reliance on the forward-looking statements contained in this Form 10-Q, which speak only as of the date hereof. Sipex disclaims any obligation to publicly update or revise any such statements to reflect any change in expectations or in events, conditions, or circumstances on which any such statements may be based, or that may affect the likelihood that actual results will differ from those set forth in the forward-looking statements.

Overview

We are a semiconductor company that designs, manufactures and markets, high performance analog integrated circuits that are used primarily by original equipment manufacturers operating in the computing, communications and networking infrastructure markets.

Critical Accounting Policies

The discussion and analysis of our financial condition and results of operations is based on our condensed consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States. The preparation of these financial statements 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 condensed consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. On an ongoing basis, we evaluate our estimates, including those significant estimates that are particularly susceptible to change, which include revenue recognition, sales returns, inventory reserves, restructuring and impairment, and income taxes. We base our estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances. There can be no assurance that actual results will not differ from those estimates.

We have identified the accounting policies below as the policies most critical to our business operations and the understanding of our results of operations. The impact and any associated risks related to these policies on our business operations is discussed throughout Management's Discussion and Analysis of Financial Condition and Results of Operations where such policies affect our reported and expected financial results.

Revenue recognition. We record revenue to our largest distributor at the time the product is sold through to the end user (sell-through). For all other product sales, assuming all other revenue recognition criteria have been met, revenue is recognized at the time of shipment because these distributors/customers have no price protection and have limited return rights. In addition, management believes that it is able to estimate and establish appropriate reserves for future returns from these distributors. For product sales recognized at the time of shipment, Sipex accrues for estimated sales returns upon shipment based upon our estimates of future returns. Revenue from engineering service contracts is recorded as performance is completed.

Sales returns. To estimate reserves for future sales returns, we regularly review our history of actual returns for each major product line. We also communicate monthly with our channel partners to gather information about sell-through activity, end user satisfaction and to determine the volume of inventory in the channel. We use the results of this analysis to estimate the reserves for sales returns. We adjust our reserves for future returns as necessary, based on returns experience, returns expectations and our communications with our channel partners.

In estimating reserves, we also consider unusual events and market conditions. It is possible that future events such as the introduction of a competitive product, product obsolescence, price competition, continued slowness in the semiconductor industry and distributors' desire to decrease levels of inventory in the distribution channel could result in significant changes in customer demand and cause future returns to increase beyond historical levels. Management believes that it is able to estimate returns and establish appropriate reserves for returns from

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customers for which Sipex recognizes revenue as of shipment, using the process described above. However, since reserves for estimated sales returns are recorded as a reduction in revenues, any significant difference between our estimated and actual returns experience, or changes in our estimate of reserves for future returns, would be reflected in our reported revenues in the period we determine that difference, and could have a material impact on our future results of operations.

Inventory reserves. We establish inventory reserves for estimated excess quantities, obsolescence or lack of marketability. In addition, we establish estimates to write down inventory costs to the lower of cost or market. The excess and obsolescence reserve is calculated by comparing current inventory to both anticipated future demand and shipment history. Lower of cost or market adjustments are determined by reviewing shipments during the quarter and comparing actual cost to anticipated market pricing. Inventories are written down to the lower of cost or market which becomes the cost basis. In establishing the reserves and estimating anticipated market pricing, we also consider current market conditions, industry performance, distributor inventory levels and sales to end-users and all other relevant factors. If actual market conditions are less favorable than those projected by management,

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additional inventory reserves may be required. Reviews of the adequacy of inventory reserves are performed on a quarterly basis.

Restructuring and impairment. The determination of the estimated restructuring accrual and impairment requires significant management judgment. To estimate the restructuring accrual, we prepare a plan that includes the number of employees to be terminated and the related severance cost, the amount of impairment for certain fixed assets and inventory, the termination costs of certain leases and the related actions required to execute the plan. It is possible that future events such as voluntary employee terminations, sublease agreements or a shift in the timing of the execution of the plan could result in significant changes to the original estimate.

Sipex reviews long-lived assets and certain identifiable intangibles, including goodwill, for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to future net cash flows expected to be generated by the asset. In estimating future net cash flows, management makes certain assumptions including future sales levels, gross profit margins and expense levels. The future net cash flows can vary from management estimates due to unforeseen circumstances which may result in an impairment or additional impairment charges required to be recognized in the income statement.

We accounted for restructuring charges prior to January 1, 2003, in accordance with Emerging Issues Task Force Issue 94-3 (EITF 94-3), Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity (including Certain Costs Incurred in a Restructuring) and SEC Staff Accounting Bulletin No. 100 (SAB 100), Restructuring and Impairment Charges. Under EITF 94-3, costs associated with restructuring activities are recorded as restructuring costs in the consolidated statement of operations. In June 2002 the FASB issued SFAS No. 146, Accounting for Costs Associated With Exit or Disposal Activities. SFAS No. 146 requires companies to recognize costs associated with exit or disposal activities when they are incurred rather than at the date of commitment to an exit or disposal plan. This Statement is effective for exit or disposal activities initiated after December 31, 2002. On January 1, 2003, the Company adopted SFAS No. 146 and at the time of adoption, there was no material impact on our financial position or results of operations; however, the Company has not yet determined the implications of adoption on future results of operations.

Income taxes. In assessing the net realizable value of deferred tax assets, management considers whether it is more likely than not that some portion or all of the deferred tax assets will not be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income during the periods in which those temporary differences become taxable. Management considers the scheduled reversals of deferred tax liabilities, projected future taxable income, and tax planning strategies in making this assessment. Based upon the level of historical taxable income and projections for future taxable income over the periods in which the deferred tax assets are deductible, management believes that it is not more likely than not that the deferred tax assets at December 31, 2002 will be realized in the future. We therefore established a full valuation allowance and incurred a tax charge for the full amount of deferred income tax asset of \$48.8 million for the year 2002. We do not have a balance for deferred tax assets at March 29, 2003.

Results of Operations

The table below presents the statements of operations for the three-month periods ended March 29, 2003 and March 30, 2002, as a percentage of net sales.

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	Three Months Ended	
	March 29, 2003	March 30, 2002
Net sales	100.0%	100.0%
Cost of sales	99.9	86.5
Gross profit	0.1	13.5
Operating expenses		
Research and development	19.4	16.9
Marketing and selling	12.7	14.1
General and administrative	13.0	10.3
Restructuring costs	0.0	0.0
Total operating expenses	45.1	41.3
Operating loss	(45.0)	(27.8)
Other income (expense), net	(1.6)	(2.4)
Loss before income taxes	(46.6)	(30.2)

Net Sales

Net sales for the first quarter of 2003 decreased 5.9% to \$15.1 million, as compared to \$16.1 million for the same period last year. The \$1.0 million decrease in net sales in the first quarter of 2003, as compared to the same period last year, was mainly due to the sale of the hybrid product family to SatCon Electronics Inc. at the end of the third quarter of 2002, which resulted in no net sales of this product family in the first quarter of 2003. This decrease was offset, in part, by increases in the sales of optics, interface and analog display product families. We also experienced a shortfall in production from one of our foundries which contributed to the decrease.

International net sales increased 1.4% and domestic net sales decreased 23.8% in the first quarter, as compared to the corresponding 2002 period. International net sales represented 76% and 71% of net sales for the first quarter of 2003 and 2002, respectively. Geographically, we experienced sales growth of 331.1% in Japan and 6.0% in the Pacific Rim, which was primarily attributable to the optics product line while sales declined 23.8% in the United States and 47.8% in Europe in the first quarter of 2003, as compared to the first quarter of 2002.

Gross Profit

Gross profit for the first quarter of 2003 decreased 99.1% to \$20,000, as compared to \$2.2 million for the same period last year. As a percentage of net sales, gross profit decreased to 0.1% for the first quarter of 2003 from 13.5% in the same prior year period. The deterioration in gross margin in the first quarter of 2003 as compared to the first quarter of 2002 was due to decreased sales and lower capacity utilization within the manufacturing fab.

Research and Development

Research and development expenses for the first quarter of 2003 increased \$219,000 or 8.1%, as compared to the same period in the previous year. The increase in research and development expense in the first quarter of 2003 was due mainly to decreased labor costs in the first quarter of 2002 due to a temporary salary cut, which was lifted later in 2002, and increased new product development costs including wafers and mask sets. As a percentage of net sales, research and development increased to 19.4% for the first quarter of 2003, as compared to 16.9% for the same period last year, which was primarily attributable to the foregoing factors as well as the decrease in revenue.

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Marketing and Selling

Marketing and selling expenses for the first quarter of 2003 decreased \$342,000, or 15.1%, as compared to the same period in the previous year. The decrease in marketing and selling expenses in the first quarter was due mainly to decreased sales representative commissions on the lower sales and decreased advertising expenses, offset, in part, by an increase in labor expenses due to severance payments. As a percentage of net sales, marketing and selling decreased to 12.7% for the first quarter of 2003, as compared to 14.1% for the same period last year.

General and Administrative

General and administrative expenses for the first quarter of 2003 increased \$314,000 or 19.0%, as compared to the same period in the previous year. The increase in the first quarter of 2003 was due mainly to decreased labor costs in the first quarter of 2002 due to a temporary salary cut, which was lifted later in 2002, and increased accounting and legal fees. As a percentage of net sales, general and administrative expenses increased to 13.0% from 10.3% during the same quarter last year.

Restructuring Costs

During the first quarter of 2003, the Company paid \$217,000 on the accrued restructuring balance of \$755,000 outstanding as of December 31, 2002. The payments consisted mainly of employee severance costs. In addition, the accrual was reduced by \$6,000 for the reversal of accrued facility exit costs. The balance of the accrual, \$532,000, as of March 29, 2003 consists of severance costs expected to be paid during the second quarter of 2003.

Other Expense, Net

Other expense, net was \$(241,000) in the first quarter of 2003 and (\$387,000) in the first quarter of 2002. The reduction in the net expense for the first quarter of 2003 from the first quarter of 2002 was due to decreased royalty expenses in the first quarter of 2003, partially offset by higher interest expenses on increased borrowings.

Income Taxes

For the first three months of 2003, income tax expense consisted of accruals for income taxes relating to our international locations. For the first three months of 2002, we recorded an income tax benefit at a 39% effective rate. We recorded the tax benefit for the 2002 period and the related increase in deferred tax assets, as we believed it was more likely than not, considering the level of historical taxable income and expectations for future taxable income, that the operating loss would be utilized in the future to offset taxable income. However, in the second quarter of 2002, we established a full valuation allowance for our deferred tax assets, as we no longer believed that it was more likely than not that the net operating loss and tax credit carryforwards would be realized during the carryforward period. This change in estimate during the second quarter of 2002 was based on updated evaluations considering historical taxable income levels and expectations of future taxable income.

Financial Condition, Liquidity and Capital Resources

As of March 29, 2003, we had available funds of \$11.7 million consisting of cash, cash equivalents and short-term investments, as compared to \$16.5 million at December 31, 2002. Net cash used in operations was \$4.3 million for the quarter ended March 29, 2003 and \$642,000 for the quarter ended March 30, 2002. Net cash used in operating activities in the first quarter of 2003 resulted primarily from a \$7.2 million net loss, of which \$2.8 million was non-cash related, and a \$3.6 million increase in accounts receivable, partially offset by a \$1.7 million decrease in inventories and a \$1.2 million decrease in prepaids and other current assets. In the first quarter of 2002, net cash used in operating activities resulted primarily from a \$3.0 million net loss, of which \$1.0 million was non-cash related, and a \$2.0 million increase in inventories, partially offset by a \$1.8 million increase in accounts payable.

Net accounts receivable was \$10.6 million and \$7.3 million as of March 29, 2003 and December 31, 2002, respectively. The \$3.3 million increase was due primarily to an increased concentration of shipments made toward the end of the first quarter of 2003. Bad debt allowances were \$281,000 and \$292,000 as of March 29, 2003 and December 31, 2002, respectively. Distributor reserves were \$619,000 and \$653,000 as of March 29, 2003 and December 31, 2002,

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respectively. The decrease was the result of continued improved inventory management and decreased inventory levels at the distributors. These improvements were offset by a reserve for OEM returns of \$166,000 which was established in the first quarter of 2003 for estimated future OEM returns.

Inventory was \$12.1 million and \$14.4 million as of March 29, 2003 and December 31, 2002, respectively. The \$2.3 million decrease in the first quarter consisted of a \$2.7 million decrease in inventory offset by a \$365,000 decrease in inventory reserves. The reductions in the inventory levels and the offsetting reserve decreases were due to a less favorable production mix on interface and power management units and the disposal of discontinued material.

Net cash provided by (used in) investing activities was \$7.6 million and (\$443,000) for the quarters ended March 29, 2003 and March 30, 2002, respectively. Additions to property, plant and equipment were \$443,000 for each of the quarters ended March 29, 2003 and March 30, 2002. Additionally in the first quarter of 2003, \$8.0 million was provided from the maturity of short-term investments, which was used to provide funding for operations.

Net cash used in financing activities was \$1.0 million for the quarter ended March 30, 2002. There was no cash used in or provided by financing activities in the first quarter of 2003. In the first quarter ended March 30, 2002, \$1.4 million was used to pay down the Company's bank line-of-credit, which was partially offset by proceeds from the issuance of the Company's common stock.

In February 1999, we filed a lawsuit against Maxim Integrated Products, Inc. (Maxim) with the U.S. District Court for the District of Massachusetts seeking a declaratory judgment that three of our products did not infringe Maxim patents. Maxim filed counterclaims alleging certain products sold by Sipex infringe a Maxim patent. The counterclaims seek injunctive relief and unspecified damages. We have denied infringement and allege that the patent is invalid. We expect to settle this lawsuit in the near future within the amounts accrued in the accompanying condensed consolidated financial statements.

We believe that our currently available cash and investments, combined with our continued cost reduction programs-in-process and the restructuring and reorganization that we have taken, will be sufficient to meet our cash and working capital requirements through at least the next twelve months. We may need to raise additional funds if our estimates change or prove inaccurate, if our cost reduction initiatives are insufficient for general working capital purposes, or to strengthen our financial position. In this regard, we recently announced that we are in discussions with Future Electronics, our only distributor in North America and Europe, regarding a strategic sales arrangement and a secured convertible note of approximately \$10 million. These discussions are preliminary, and there can be no assurance that the proposed transactions will be consummated on terms favorable to the Company or at all.

Our ability to raise funds may be adversely affected by a number of factors relating to our company, as well as factors beyond our control, including the continued downturn in the semiconductor industry, volatility and uncertainty in the capital markets as well as continued market uncertainty related to the ongoing U.S. war on terrorism. There can be no assurance that any financing, including the proposed financing with Future Electronics, will be available on terms acceptable to us, if at all, and any need to raise additional capital through the issuance of equity or debt securities may result in additional, and perhaps, significant dilution.

Factors Affecting Future Results

Except for historical information contained herein, the matters set forth on this report on Form 10-Q, including the statements in the following paragraphs, are forward looking statements that are dependent on certain risks and uncertainties including, without limitation, such factors as, among others, delays in new product and process technology announcements and product introductions by us or our competitors, competitive pricing pressures, fluctuations in manufacturing yields, changes in the mix or markets in which our products are sold, availability and costs of raw materials, reliance on subcontractors, the cyclical nature of the semiconductor industry, industry-wide wafer processing capacity, political and economic conditions in various geographic areas, and costs associated with other events, such as under-utilization or expansion of production capacity, intellectual property disputes, litigation, or environmental regulation and other factors described below and elsewhere in this Form 10-Q. These risks and uncertainties are not the only ones facing our company. Additional risks and uncertainties not presently known to us or that we currently deem immaterial may also impair our business operations. If any of these risks actually occur, our business, financial condition or results of operations could be materially adversely affected. In such case, the trading price of our common stock could decline.

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Our quarterly and annual operating results are volatile and difficult to predict and may cause our stock price to fluctuate.

Our quarterly and annual operating results are affected by a wide variety of factors that could materially and adversely affect net sales and profitability from period-to-period, including:

- the cyclical nature of the semiconductor industry;
- competitive pressures on selling prices;
- the timing and cancellation of customer orders;
- the availability of foundry capacity, raw materials and assembly and test capacity;
- fluctuations in yields;
- changes in product mix;
- our ability to introduce new products and technologies on a timely basis;
- the introduction of products and technologies by our competitors;
- market acceptance of our products and our customers' products;
- the level of orders received that can be shipped in a quarter;
- delays in shipments from our fabrication plant to assembly houses;
- our ability to manufacture in the correct mix to respond to orders on hand and new orders received in the future;
- the timing of investments in research and development, including tooling expenses associated with product development, process improvements and production;
- the level of future product returns; and
- the overall economic conditions in the United States and abroad, particularly as a result of the ongoing U.S. war on terrorism.

Due to the absence of substantial non-cancelable backlog, we typically plan our production and inventory levels based on internal forecasts of customer demand, which are highly unpredictable and can fluctuate substantially.

Our expense levels are based, in part, on expectations of future revenues and are, to a large extent, fixed in the short term. Our future revenues are difficult to predict and at times in the past we have failed to achieve revenue expectations. We may be unable to adjust spending in a timely manner to compensate for any unexpected revenue shortfall. If revenue levels are below expectations for any reason, operating results are likely to be unfavorably affected. We may also take steps to adjust our strategic product families and change our cost structure, which may result in our incurring additional restructuring, reorganization and other charges. Based on forecasts, we may increase our operating expenses for personnel and new product development and for inventory in anticipation of increasing sales levels; therefore, operating results would be worsened if increased sales are not achieved. In addition, we are limited in our ability to reduce costs quickly in response to any revenue shortfalls.

Since 2001, the semiconductor industry has been experiencing a prolonged and severe downturn that continues to adversely affect our results of operations. Our net sales for the quarter ended March 29, 2003 decreased 5.9% from the corresponding prior year period and 8.8% from the quarter ended December 31, 2002. Our business depends on market demand for products using analog semiconductors. Prolonged downturns in the semiconductor industry lead to decreases in net sales levels and may cause continued losses and cash flow shortages.

As a result of the foregoing and other factors, we may experience material fluctuations in future operating results on a quarterly or annual basis, which could substantially negatively affect our business, financial condition and operating results.

If we are unable to promptly and effectively implement adequate controls, systems and procedures, we may continue to experience weaknesses in our internal controls and operations that could call into question the accuracy of our financial results and we may be unable to achieve Section 404 Certification as mandated under the Sarbanes-Oxley Act.

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As a result of the December 31, 2002 audit of the consolidated financial statements, our auditors noted certain matters involving internal control and its operation that they considered to be material weaknesses under standards established by the American Institute of Certified Public Accountants. Material weaknesses are significant

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deficiencies in the design or operation of internal control that could adversely affect our ability to record, process, summarize and report financial data consistent with the assertions of management in the financial statements. By definition, material weaknesses do not reduce to a relatively low level the risk that errors or fraud, in amounts that would be material in relation to the financial statements being audited, may occur and may not be detected within a timely period by employees in the normal course of performing their assigned functions. The material weaknesses noted during the audit resulted from the deficiencies in the systems and processes used in the preparation of the financial statements and the lack of proper management review and account analysis in certain areas. Although other areas were impacted by the material weaknesses, the most significant issues arising from the material weaknesses included inappropriate process and systems tracking of inventory, including significant manual reconciliations, as well as inappropriate and insufficient analysis performed in evaluating inventory costs capitalized and inventory excess and obsolete reserves established. To ensure appropriate analysis, we must systemize processes by establishing appropriate guidelines that will reduce the level of manual reconciliations, as well as improve the account analysis methodologies and increase the level of supervisory and management review.

While we have identified and have begun to take measures to improve our systems and internal control structure, implement more rigorous internal accounting and operational policies, procedures and controls, and conduct systems training, the success of these measures cannot be assured and will depend on many factors, including our ability to hire, train and retain additional qualified accounting staff. Our ability to implement our business plan successfully in a volatile market requires effective management systems and a system of financial processes and controls. If we are unable to maintain an adequate level of processes and controls and improve our systems, we may not be able to accurately report our financial performance on a timely basis and our business and stock price would be adversely affected. In addition, we may be unable to achieve Section 404 certification as mandated by the Sarbanes-Oxley Act.

We have recently experienced significant changes in senior management and our corporate organization.

A number of members of our senior management team, including our Chief Executive Officer and President, Senior Vice President of Operations; Senior Vice President of Finance and Chief Financial Officer; Senior Vice President, Marketing and Business Development; Vice President of Engineering and Vice Presidents of Sales for Asia and the Americas have joined our company since the second half of 2002. In particular, our Chief Financial Officer, Phillip Kagel, joined Sipex in February 2003, after the audit of our financial statements for the year ended December 31, 2002 was substantially complete. Changes in management may be disruptive to our business and may result in the departure of existing employees and/or customers. In addition, during the third quarter of 2002, we announced the restructuring and reorganization of the Company into six functional groups reporting to our Chief Executive Officer, as well as the sale of our hybrid product family. It may take significant time to integrate our new management personnel and achieve efficiencies from our new corporate structure, which may adversely affect our business and operating results.

We may experience difficulties in developing and introducing new or enhanced products necessitated by technological advances.

Our future success will depend, in part, upon our ability to anticipate changes in market demand and evolving technologies. To remain competitive, we must enhance our current products and develop and introduce new products that keep pace with technological advancements and address the increasingly sophisticated needs of our customers. Our products may be rendered obsolete if we fail to anticipate or react to change, and, as a result, our revenues and cash flow may be negatively impacted. Our success depends on our ability to develop new semiconductor devices for existing and new markets, to introduce these products in a timely manner and to have these products selected for design into new products of our customers. The development of these new devices is highly complex and from time to time we have experienced delays in completing the development of new products. Successful product development and introduction depends on a number of factors, including:

- accurate new product definition;
- timely completion and introduction of new product designs;
- availability of foundry capacity;
- achievement of manufacturing yields; and
- market acceptance of our products and our customers' products.

Our success also depends upon our ability to accurately specify and certify the conformance of our products to applicable standards and to develop our products in accordance with customer requirements. There can be no

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assurance that we will be able to adjust to changing market conditions as quickly and cost-effectively as necessary to compete successfully. There can be no assurance that we will be able to introduce new products in a timely and cost-effective manner or in sufficient quantities to meet customer demand or that these products will achieve market acceptance. Furthermore, there can be no assurance that our customers' products will achieve market acceptance.

We depend on distributors who sell directly to OEMs.

Approximately 83% of our net sales in the first quarter of 2003 are from shipments of our product to distributors who sell directly to OEMs. Our agreements with distributors contain limited provisions for return of our product, including stock rotations whereby distributors may return a percentage of their product based upon a percentage of their most recent six months shipments (except for Future Electronics, which is based on three months). In addition, in certain circumstances upon termination of the distributor relationship distributors may return a percentage of purchases. The loss of business from any of our significant distributors or the delay of significant orders from any of them, even if only temporary, could significantly reduce our income, delay recognition of revenue and impact our ability to accurately predict cash flow. We estimate the amount of future returns and have established reserves for estimated returns based upon information including sales during the period into the distribution channel, reported sell-through by distributors to OEMs, distributor inventory levels and the specific terms of the distributor agreements as well as historical returns experience. We defer revenue on shipments to Future Electronics until the product is resold by the distributor to the end user (sell-through), because the arrangement with this distributor includes price concessions and return rights the potential impact of which we believe we cannot reasonably estimate.

We derive a substantial portion of our revenues from Future Electronics, and our revenues would likely decline significantly if Future Electronics elects not to make, cancels, reduces or defers purchases of our products.

Future Electronics has historically accounted for a significant portion of our revenues. It is our largest distributor worldwide, and accounted for 30% of total net sales for the first quarter of 2003 and 24%, 21% and 23% of total net sales, respectively, for the years ended December 31, 2002, 2001 and 2000. We anticipate that sales of our products to Future Electronics will continue to account for a significant portion of our revenues. The loss of Future Electronics as a distributor, or a significant reduction in orders from Future Electronics would materially and adversely affect our operating results, our business, our financial condition and our stock price.

We have a distributor agreement with Future Electronics that provides for Future Electronics to act as our sole distributor for certain products within North America and Europe. Sales to this distributor are made under an agreement that provides protection against price reduction for their inventory of Sipex products. Sipex maintains a separate price list for products sold to Future Electronics, which reflects discounts from the prices charged to customers in direct sales transactions. Our distributor agreement with Future Electronics does not contain minimum purchase commitments. As a result, Future Electronics could cease purchasing our products with short notice to us. In addition, Future Electronics may defer or cancel orders without penalty, which would likely cause our revenues, our business, our financial condition and our stock price to decline.

As recently announced, we have commenced discussions with Future Electronics regarding a strategic sales arrangement and a secured convertible note of approximately \$10 million. The discussions are preliminary and any terms and conditions of the sales arrangement and the note remain subject to negotiation of a definitive agreement, board approval and potential regulatory approvals. There can be no assurance that the proposed transactions will be consummated on terms favorable to the Company or at all.

We may not successfully expand our sales and distribution channels.

An integral part of our strategy is to expand our sales and distribution channels. We are increasing resources dedicated to developing and expanding these channels but we may not be successful doing so. If we are successful in increasing our sales through indirect sales channels, we expect that those sales will be at lower per unit prices than sales through direct channels, and revenues we receive for each sale will be less than if we had sold the same product to the customer directly. Selling through indirect channels may also limit our contact with our customers. As a result, our ability to accurately forecast sales, evaluate customer satisfaction and recognize emerging customer requirements may be hindered. Even if we successfully expand our distribution channels, any new distributors may not have the technical expertise required to market and support our products successfully. If parties do not provide adequate levels of services and technical support, our customers could become dissatisfied, we could be required to devote additional resources for customer support, and our brand name and reputation could be negatively impacted. Our

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strategy of marketing products directly to our customers and indirectly through distributors may result in distribution channel conflicts. Our direct sales efforts may compete with those of our indirect channels and, to the extent different distributors target the same customers, distributors may also compete with each other. Although we have attempted to manage our distribution channels to avoid potential conflicts, channel conflicts may negatively impact our relationships with existing sales representatives or distributors or impair our ability to attract sales representatives.

We may face significant risks related to our international operations.

We derive a significant portion of our net sales from international sales, including Asia, which are subject to certain risks, including:

- unexpected changes in legal and regulatory requirements;
- changes in tariffs;
- exchange rates and other barriers;
- political and economic instability;
- difficulties in accounts receivable collection;
- difficulties in managing distributors or representatives;
- difficulties in staffing and managing international operations;
- difficulties in protecting our intellectual property overseas;
- the seasonality of sales; and
- potentially adverse tax consequences.

In addition, recent uncertainty associated with severe acute respiratory syndrome, or SARS, has adversely affected business conditions in general and inhibited business travel. Concerns regarding SARS could result in decreased demand for our product and negatively impact product shipments and bookings.

Our international sales in the first quarter of 2003 were \$11.6 million or 76% of total net sales and \$50.5 million and \$44.4 million for the years ended 2002 and 2001, respectively, or 76% and 62% of total net sales, respectively. There can be no assurance that economic and geopolitical troubles in any area of the world will not have a material adverse effect on our business, results of operations and financial condition.

Our inability to meet any increase in demand could reduce our market share.

Demand shifts in the semiconductor industry are rapid and difficult to predict, and we may not be able to respond quickly enough to an increase in demand, if any. Our ability to increase sales of our products depends, in part, upon our ability to optimize the use of our manufacturing capacity in a timely manner and, if necessary, expand our manufacturing capacity. If we are unable to respond to rapid increases in demand, if any, for our products on a timely basis or to manage any corresponding expansion of our manufacturing capacity effectively, our customers could increase their purchases from our competitors, which would reduce our market share.

Our financial results may be adversely affected due to the highly volatile optical storage market.

A significant component of the company's growth strategy depends on increasing shipments in the optical storage market. During the first quarter of 2003 and the year ended December 31, 2002, we derived all of our optical storage sales from a limited number of customers in Japan. Local suppliers in Japan may have a competitive advantage over Sipex, which could adversely affect our ability to grow sales or continue to compete in Japan or other regions of the world. Any failure to increase our shipments in the optical storage market could limit our ability to grow our business and could adversely affect our operating results.

If we are unable to compete effectively with existing or new competitors, we will experience fewer customer orders, reduced revenues, reduced gross margins and lost market share.

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We compete in markets that are intensely competitive, and which are subject to both rapid technological change and continued price erosion. Our competitors include many large domestic and foreign companies that have substantially greater financial, technical and management resources than us. Loss of competitive position could result in price reductions, fewer customer orders, reduced revenues, reduced gross margins and loss of market share, any of which would affect our operating results and financial condition. To remain competitive, we continue to evaluate our manufacturing operations, looking for additional cost savings and technological improvements. If we are not able to successfully implement new process technologies and to achieve volume production of new products at acceptable

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yields, our operating results and financial condition may be affected. In addition, if competitors in Asia reduce prices on commodity products, it would adversely affect our ability to compete effectively in that region. Our future competitive performance depends on a number of factors, including our ability to:

- accurately identify emerging technological trends and demand for product features and performance characteristics;
- develop and maintain competitive products;
- enhance our products by adding innovative features that differentiate our products from those of our competitors;
- bring products to market on a timely basis at competitive prices;
- respond effectively to new technological changes or new product announcements by others;
- increase device performance and improve manufacturing yields;
- adapt products and processes to technological changes; and
- adopt and/or set emerging industry standards.

There can be no assurance that our design, development and introduction schedules for new products or enhancements to our existing and future products will be met. In addition, there can be no assurance that these products or enhancements will achieve market acceptance, or that we will be able to sell these products at prices that are favorable to us.

We have only limited protection for our proprietary technology.

The semiconductor industry is characterized by frequent litigation regarding patent and other intellectual property rights. Although we are not aware of any pending or threatened patent litigation that we consider material, there can be no assurance that third parties will not assert claims against us with respect to existing or future products or technologies and we have been subject to such claims in the past. In litigation to determine the validity of any third party claims, such litigation, whether or not determined in our favor, could result in significant expense to us and divert the efforts of our management personnel from productive tasks. In the event of an adverse ruling in such litigation, we may be required to discontinue the use of certain processes, cease the manufacture, use and sale of infringing products, expend significant resources to develop non-infringing technology or obtain licenses to the infringing technology. There can be no assurance that licenses will be available on acceptable terms, or at all, with respect to disputed third party technology. In the event of a successful claim against us and our failure to develop or license a substitute technology at a reasonable cost, our business, financial condition and results of operations would be materially and adversely affected.

In February 1999, we filed a lawsuit against Maxim Integrated Products, Inc. (Maxim) with the U.S. District Court for the District of Massachusetts seeking a declaratory judgment that three of our products did not infringe Maxim patents. Maxim filed counterclaims alleging certain products sold by Sipex infringe a Maxim patent. The counterclaims seek injunctive relief and unspecified damages. We have denied infringement and allege that the patent is invalid. We expect to settle this lawsuit in the near future within the amounts accrued in the accompanying condensed consolidated financial statements.

There can be no assurance that foreign intellectual property laws will protect our intellectual property rights. Furthermore, there can be no assurance that others will not independently develop similar products, duplicate our products or design around any of our patents. We may be subject to, or may initiate, interference proceedings in the U.S. patent office, which can demand significant financial and management resources.

Our future success depends on retaining our key personnel and attracting and retaining additional highly qualified employees.

Our success depends upon the continued service of our executive officers and other key management and technical personnel, and on our ability to continue to attract, retain and motivate qualified personnel, such as experienced analog circuit designers. The competition for these employees is intense. Most of our employees are employees at-will and we have no fixed-term employment agreements with most employees, which means that they can terminate their employment at any time. There can be no assurance that we will be able to retain our design engineers, executive officers and other key personnel. The loss of the services of one or more of our design engineers, executive officers or other key personnel or our inability to recruit replacements for these personnel or to otherwise attract, retain and motivate qualified personnel could seriously impede our success.

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Our manufacturing processes are very complex, which may result in manufacturing difficulties.

Our manufacturing processes are highly complex and are continuously being modified in an effort to improve yields and product performance. Process changes can result in interruptions in production or significantly reduced yields causing product introduction or delivery delays. In addition, yields can be adversely affected by minute impurities in the environment or other problems that occur in the complex manufacturing process. Many of these problems are difficult to diagnose and are time-consuming or expensive to remedy. From time to time we have experienced unfavorable yield variances. In particular, new process technologies or new products can be subject to especially wide variations in manufacturing yields and efficiency. There can be no assurance that our foundry or those of our suppliers will not experience unfavorable yield variances or other manufacturing problems that result in delayed product introduction or delivery delays.

We rely on outside foundries to supply wafers and those foundries may not produce at acceptable levels.

We rely on outside foundries to supply fully processed semiconductor wafers. This reliance on outside foundries presents the following potential risks:

lack of adequate wafer supply;

limited control over delivery schedules;

unavailability of or delays in obtaining access to key process technologies; and

limited control over quality assurance, manufacturing yields and production costs.

Additionally, the manufacture of integrated circuits is a highly complex and technologically demanding process. Our third party foundries have, from time to time, experienced lower than anticipated manufacturing yields, particularly in connection with the introduction of new products and the installation and start-up of new process technologies. There can be no assurance that our outside foundries will not experience lower than expected manufacturing yields in the future.

Additionally, we do not have a guaranteed level of production capacity at any of these foundries. The ability of each foundry to provide wafers to us is limited by the foundry's available capacity, and the foundry's allocation of its available capacity among multiple customers. There can be no assurance that our third party foundries will allocate sufficient capacity to satisfy our requirements. We have experienced decreased allocations of wafer supplies from our suppliers in the past, which reduced our capacity to ship products, and, thus, recognize revenues. Additionally, any sudden reduction or elimination of any primary source or sources of fully processed wafers could result in a material delay in the shipment of our products. If any other delays or shortages occur in the future, our business and operating results will be negatively impacted.

Our wafer fabrication facility and the facilities of certain of our significant customers and third party wafer suppliers are located in areas susceptible to earthquakes.

Our in-house fabrication facility and the facilities of certain of our significant customers and third-party wafer suppliers are located in areas that are susceptible to earthquakes. Damage caused by earthquakes may result in shortages in water or electricity or transportation, which could limit the production capacity of our wafer facility and/or the ability of certain of our subcontractors to provide needed products. Any reduction in production capacity or the ability to obtain fully processed semiconductor wafers could cause delays or shortages in our product supply, which would negatively impact our business. If our facilities or the facilities of our customers are damaged by future earthquakes, it could have a materially adverse effect on our business.

We rely on outside suppliers to assemble, test and ship product to our customers.

We rely on outside assembly houses to assemble, test and ship our product to end customers. There can be no assurance that our third party suppliers will allocate sufficient capacity to us to meet our requirements. Any sudden reduction or elimination of a primary source could result in material delay in the shipment of our product and could have a material adverse affect on our business and operating results.

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We have limited control over quality assurance, manufacturing yields and production costs. We have in the past experienced yield issues and delays. We could experience delays or yield issues in the future due to the transfer of products from development to production, which could negatively impact our business and operating results.

We must comply with significant environmental regulations, which is difficult and expensive.

We are subject to a variety of federal, state and local governmental regulations related to the use, storage, discharge and disposal of toxic, volatile or otherwise hazardous chemicals used in our manufacturing processes. Although we believe that our activities conform to presently applicable environmental regulations, the failure to comply with present or future regulations could result in fines being imposed on us, suspension of production or a cessation of operations. Any failure by us to control the use of, or adequately restrict the discharge of, hazardous substances, or otherwise comply with environmental regulations, could subject us to significant future liabilities. In addition, there can be no assurance that we have not violated laws or regulations in the past, which violations could result in remediation or other significant liabilities, or that past use or disposal of environmentally sensitive materials in conformity with then existing environmental laws and regulations will not result in remediation or other significant liabilities under current or future environmental laws or regulations.

It would be difficult for us to adjust our spending significantly if we experience any revenue shortfalls.

Our future revenues are difficult to predict and at times in the past we have failed to achieve our revenue expectations. Our expense levels are based in part, on our expectations of future revenues, and expense levels are, to a large extent, fixed in the short term. Since the fourth quarter of 2000, we have adjusted our spending levels as a result of decreased revenues and continue to focus on controlling costs. We may, however, be unable to adjust spending in a timely manner to compensate for any unexpected revenue shortfall. If revenue levels are below expectations for any reason our operating results will be negatively impacted. Due to the absence of substantial non-cancelable backlog, we typically plan our production and inventory levels based on internal forecasts of customer demand, which are highly unpredictable and often fluctuate substantially. In the future, if we believe that demand is increasing, our operating expenses for personnel, new product development and for inventory would correspondingly increase as needed in anticipation of increasing sales levels. Our operating results would be negatively impacted if increased sales were not achieved. In addition, we are limited in our ability to reduce costs quickly in response to any revenue shortfalls.

We may have capital requirements to maintain and grow our business and we may not be able to secure adequate capital on acceptable terms.

In order to remain competitive, we must continue to make investments in our facilities and capital equipment. We have obtained additional funding through the private placement of 3.0 million shares of Sipex common stock on April 16, 2002, which provided \$23.5 million to the Company, net of placement agent fees and other costs of issuance, and through the private placement of a convertible secured note and related warrant on September 27, 2002, which provided approximately \$12.0 million to the Company, net of costs of issuance. We may need to seek additional equity or debt financing from time to time and cannot be certain that additional financing will be available on favorable terms, if at all. In this regard, as recently announced, we have commenced discussions with Future Electronics, Inc. regarding a strategic sales arrangement and a secured convertible note of approximately \$10 million. The note would have conversion rights contingent upon Future Electronics' attainment of predetermined sales levels over specified periods of time. The discussions are preliminary and any terms and conditions of the sales arrangement and the note remain subject to negotiation of a definitive agreement, board approval and potential regulatory approvals. There can be no assurance that the proposed transactions will be consummated on terms favorable to the Company or at all. Because our stock is trading near historically low levels, any future equity or convertible debt financing may result in substantial dilution to existing stockholders, depending on the price at which the equity is sold or the debt is converted and the extent of our needs. Our ability to raise funds may be adversely affected by a number of factors relating to Sipex, as well as factors beyond our control, such as capital market uncertainty and general economic conditions.

Our stock price has been volatile and could continue to remain volatile.

The trading price of our common stock is subject to wide fluctuations in response to quarter-to-quarter variations in operating results, announcements of technological innovations or new products by us or our competitors, general conditions in the semiconductor manufacturing and electronic markets, changes in earnings estimates by analysts, or other events or factors. In addition, the public stock markets have experienced extreme price

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and trading volume volatility in recent months. In the quarter ended December 31, 2000, our stock closing price ranged from a high of \$45.125 to a low of \$15.875. In the first quarter of 2003, our stock closing price ranged from a high of \$3.70 to a low of \$2.23. This volatility has significantly affected the market prices of securities of many technology companies for reasons frequently unrelated to the operating performance of the specific companies. These broad market fluctuations may adversely affect the market price of our common stock.

We could face securities litigation if our stock price remains highly volatile.

In the past, securities class action litigation has often followed periods of volatility in the market price of a company's securities. In the past, we were named in two virtually identical securities class action lawsuits. The complaints and unspecified damages alleged, among other things, that our financial statements for the second and third quarters of fiscal year 2000 contained incorrect statements. On April 12, 2002, the U.S. District Court dismissed both suits with prejudice.

The litigation process is inherently uncertain and unpredictable, however, and there can be no guarantee that we will not become subject to such suits in the future. Moreover, there can be no guarantee that if we do become subject to such suits, that the ultimate outcome will be similar to the cases noted above. Any litigation could result in substantial costs and a diversion of management's attention and resources, which could negatively impact our business.

Changes in laws, regulations and financial accounting standards may affect our reported results of operations.

The recently enacted Sarbanes-Oxley Act of 2002 and related regulations may result in changes in accounting standards or accepted practices within our industry. New pronouncements and varying interpretations of pronouncements have occurred in the past and are likely to occur in the future as a result of recent Congressional and regulatory actions. New laws, regulations, and accounting standards, as well as the questioning of, or changes to, currently accepted accounting practices in the technology industry may adversely affect our reported financial results, which could have an adverse effect on our stock price. Proposals have been made concerning the expensing of stock options which could result in rules or laws that may adversely affect our reported financial results and have an adverse effect on our stock price.

Item 3. Quantitative and Qualitative Disclosures about Market Risk:

Market Risk

Sipex invests excess cash in financial investments that are sensitive to market risks as part of its investment strategy. None of these market-sensitive instruments are held for trading purposes. Sipex does not own derivative financial instruments in its portfolio. The investment portfolio contains instruments that are subject to the risk of a decline in interest rates. As required by Sipex's investment policy, available funds are invested in a manner that assures maximum safety and liquidity and, secondarily, maximizes yield within such constraints.

Investment Rate Risk

The Company's financial investments consist primarily of high quality commercial paper and money market funds. The Company does not believe that it has a material exposure to interest rate risk.

Item 4. Controls and Procedures

During the 90 day period prior to the filing of this quarterly report, we carried out an evaluation under the supervision and with the participation of our senior management, including Walid Maghribi, our Chief Executive Officer, and Phillip A. Kagel, our Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures. Senior management and our Audit Committee have been informed by our independent auditors that they had identified material weaknesses (as defined under standards established by the American Institute of Certified Public Accountants) relating to the deficiencies in the systems and processes used in the preparation of the financial statements and the lack of proper management review and account analysis.

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Mr. Maghribi and Mr. Kagel determined that these material weaknesses, together with certain other deficiencies, if unaddressed, could result in accounting errors and impair our ability to accurately report our financial results in a timely manner.

Based on the above and under the direction of the Audit Committee and the Board of Directors, senior management have dedicated resources and are taking steps to strengthen control processes in order both to identify and rectify the deficiencies and prevent the situations from recurring. To this end, we are taking, or have taken, the following steps:

we hired Mr. Kagel as our Chief Financial Officer effective February 10, 2003;

we elected a new independent director to our Board of Directors, Joseph Consoli, who has extensive financial background and serves as the Chairman of the Audit Committee;

we established a Disclosure Committee with a mandate to assist our Chief Executive Officer and Chief Financial Officer in overseeing the accuracy and timeliness of our public disclosures and in evaluating regularly our disclosure controls and procedures;

we implemented procedures to ensure accurate and timely account analysis and reconciliations; and

updated written policies and procedures are being prepared to standardize and improve processes, including procedures relating to systems, finance policies and internal controls.

We continue to evaluate further improvements, including formalizing our processes, procedures and policies, to our internal controls and disclosure controls and procedures.

As a result of the steps taken to improve controls and following the conclusion of our recently completed review of our financial accounts, Mr. Maghribi and Mr. Kagel concluded that the information required to be disclosed in this quarterly report has been recorded, processed, summarized and reported as required. Based upon and as of the date of their evaluation, the Chief Executive Officer and Chief Financial Officer further concluded that our disclosure controls and procedures, taking into account the steps listed above to improve the controls and procedures, are effective in all material respects.

Other than as described above, there have been no significant changes in our internal controls or in other factors that could significantly affect these controls subsequent to the date of the evaluation.

Part II: OTHER INFORMATION

Item 1. Legal Proceedings

In February 1999, we filed a lawsuit against Maxim Integrated Products, Inc. (Maxim) with the U.S. District Court for the District of Massachusetts seeking a declaratory judgment that three of our products did not infringe Maxim patents. Maxim filed counterclaims alleging certain products sold by Sipex infringe a Maxim patent. The counterclaims seek injunctive relief and unspecified damages. We have denied infringement and allege that the patent is invalid. We expect to settle this lawsuit in the near future within the amounts accrued in the accompanying condensed consolidated financial statements.

Item 2. Changes in Securities and Use of Proceeds

None.

Item 3. Defaults Upon Senior Securities

None.

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

None.

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Item 5. Other Information

None.

Item 6. Exhibits and Reports on Form 8-K

(a) Exhibits

<u>Exhibit Number</u>	<u>Title</u>
99.1	Section 906 Certification
99.2	Section 906 Certification

(b) Reports on Form 8-k

None.

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SIGNATURES

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

SIPEX CORPORATION

DATE: May 13, 2003

BY

/s/ Phillip A. Kagel

Phillip A. Kagel
Senior Vice President, Finance
Chief Financial Officer & Treasurer
(Duly Authorized Officer &
Principal Financial Officer)

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Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

I, Walid Maghribi, President and Chief Executive Officer of Sipex Corporation, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Sipex Corporation;
2. Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this quarterly report;
3. Based on my knowledge, the financial statements, and other financial information included in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this quarterly report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the registrant and we have:
 - a. designed such disclosure controls and procedures to ensure that material information relating to the registrant, including its subsidiaries, is made known to us by others within those entities, particularly during the period in which this quarterly report is being prepared;
 - b. evaluated the effectiveness of the registrant's disclosure controls and procedures as of a date within 90 days prior to the filing date of this quarterly report (the Evaluation Date); and
 - c. presented in this quarterly report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent function):
 - a. all significant deficiencies in the design or operation of internal controls which could adversely affect the registrant's ability to record, process, summarize and report financial data and have identified for the registrant's auditors any material weaknesses in internal controls; and
 - b. any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls; and
6. The registrant's other certifying officer and I have indicated in this quarterly report whether or not there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

Date: May 13, 2003

By: /s/ Walid Maghribi

Walid Maghribi
President and Chief Executive Officer

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Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

I, Phillip A. Kagel, Senior Vice President, Finance, Chief Financial Officer and Treasurer of Sipex Corporation, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Sipex Corporation;
2. Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this quarterly report;
3. Based on my knowledge, the financial statements, and other financial information included in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this quarterly report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the registrant and we have:
 - a. designed such disclosure controls and procedures to ensure that material information relating to the registrant, including its subsidiaries, is made known to us by others within those entities, particularly during the period in which this quarterly report is being prepared;
 - b. evaluated the effectiveness of the registrant's disclosure controls and procedures as of a date within 90 days prior to the filing date of this quarterly report (the Evaluation Date); and
 - c. presented in this quarterly report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent function):
 - a. all significant deficiencies in the design or operation of internal controls which could adversely affect the registrant's ability to record, process, summarize and report financial data and have identified for the registrant's auditors any material weaknesses in internal controls; and
 - b. any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls; and
6. The registrant's other certifying officer and I have indicated in this quarterly report whether or not there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

Date: May 13, 2003

By: /s/ Phillip A. Kagel

Phillip A. Kagel
Senior Vice President, Finance
Chief Financial Officer and Treasurer

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EXHIBIT INDEX

Exhibit Number	Title
99.1	Section 906 Certification
99.2	Section 906 Certification