SIPEX CORP
Form 10-Q
November 17, 2003

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended September 27, 2003
or

o **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)

Delaware **(State or Other Jurisdiction of Incorporation or Organization)**	**04-6135748** **(I.R.S. Employer Identification No.)**
233 South Hillview Drive, Milpitas, California **(Address of principal executive offices)**	**95035** **(Zip Code)**

(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 x No o

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

There were 28,257,100 shares of the Registrant s Common Stock issued and outstanding as of November 7, 2003.

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Part I: FINANCIAL INFORMATION

Item 1: Financial Statements

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

	September 27, 2003	December 31, 2002
ASSETS		
Current assets:		
Cash and cash equivalents	$ 10,206	$ 6,489
Short-term investment securities	6,486	9,980
Accounts receivable, net	8,058	7,278
Accounts receivable, net, related party (note 3)	3,069	
Inventories, net	15,094	14,393
Prepaid expenses and other current assets	2,543	3,446
Total current assets	45,456	41,586
Property, plant, and equipment, net	51,766	56,997
Other assets	456	203
Total assets	$ 97,678	$ 98,786
LIABILITIES AND SHAREHOLDERS EQUITY		
Current liabilities:		
Accounts payable	$ 6,365	$ 8,103
Accrued expenses	4,728	3,570
Accrued restructuring costs		755
Deferred income, related party (note 3)	4,006	1,383
Total current liabilities	15,099	13,811
Long-term debt, related party (note 3)	21,244	10,455
Total liabilities	36,343	24,266
Commitments (Note 9)		
Shareholders equity: Preferred stock, $0.01 par value, 1,000 shares authorized and no shares issued or outstanding		
Common stock, $0.01 par value, 60,000 shares authorized; 28,216 and 28,031 shares issued and outstanding at September 27, 2003 and December 31, 2002, respectively	282	280
Additional paid-in capital	177,450	175,489
Accumulated deficit	(116,384)	(101,179)
Accumulated other comprehensive loss	(13)	(70)
Total shareholders equity	61,335	74,520

Total liabilities and shareholders equity	$ 97,678	$ 98,786

See accompanying notes to consolidated financial statements

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

	Three Months Ended		Nine Months Ended	
	September 27, 2003	**September 28, 2002**	**September 27, 2003**	**September 28, 2002**
Net sales	$ 10,462	$ 16,625	$ 31,273	$ 49,677
Net sales, related party (note 3)	5,950		15,146	
Net sales, before fair value of debt conversion rights	16,412	16,625	46,419	49,677
Fair value of debt conversion rights, related party (note 3)	(1,214)		(1,214)	
Total net sales	15,198	16,625	45,205	49,677
Cost of sales	7,881	21,272	27,215	54,092
Cost of sales, related party (note 3)	3,748		12,246	
Restructuring costs		1,909	(37)	1,909
Total cost of sales	11,629	23,181	39,424	56,001
Gross profit (loss)	3,569	(6,556)	5,781	(6,324)
Operating expenses:				
Research and development	3,377	3,407	9,738	9,680
Marketing and selling	1,759	1,813	5,126	6,286
General and administrative	1,563	1,816	5,679	6,116
Reorganization		1,623		1,623
Restructuring and facility exit costs	(29)	3,806	(329)	3,806
Impairment charges		1,819		1,819
Impairment of goodwill				2,984
Total operating expenses	6,670	14,284	20,214	32,314
Loss from operations	(3,101)	(20,840)	(14,433)	(38,638)
Interest income	31	45	96	120
Interest expense	(216)		(556)	(81)
Other expense, net	(32)	(102)	(21)	(813)
Total other expense, net	(217)	(57)	(481)	(774)
Loss before income taxes	(3,318)	(20,897)	(14,914)	(39,412)
Income tax expense	27	178	291	32,113
Net loss	$ (3,345)	$ (21,075)	$ (15,205)	$ (71,525)

Net loss per common share basic and diluted	$ (0.12)	$ (0.75)	$ (0.54)	$ (2.66)
Weighted average common shares outstanding basic and diluted	28,145	27,955	28,077	26,920

See accompanying notes to consolidated financial statements

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SIPEX CORPORATION
CONSOLIDATED STATEMENTS OF CASH FLOWS
(In thousands)
(Unaudited)

	Nine Months Ended	
	September 27, 2003	September 28, 2002
Operating activities:		
Net loss	$(15,205)	$(71,525)
Adjustments to reconcile net loss to net cash used in operating activities:		
Fair value of debt conversion rights (note 3)	1,214	
Deferred income taxes		31,851
Provision (reversal) for uncollectible receivables and returns and allowances	(604)	1,890
Fixed asset impairment loss	649	
Stock compensation expense	56	
(Gain) loss on fixed asset disposition	196	(123)
Depreciation and amortization	5,799	9,160
Impairment charges		1,819
Restructuring and reorganization charges		7,338
Amortization of discount on long-term debt, related party (note 3)	242	
Changes in current assets and liabilities:		
Accounts receivable	(3,245)	(837)
Inventories, net	(701)	3,732
Prepaid expenses and other current assets	903	(142)
Other assets	(138)	
Accounts payable	(1,738)	4,961
Accrued expenses	1,158	1,180
Accrued restructuring costs	(755)	
Deferred income, related party (note 3)	2,623	100
Net cash used in operating activities	(9,546)	(10,596)
Investing activities:		
Purchase of short-term investment securities	(7,469)	
Proceeds from maturity of short-term investment securities	10,963	(5,994)
Purchase of property, plant and equipment	(1,413)	(3,569)
Net cash provided by (used in) investing activities	2,081	(9,563)
Financing activities:		
Debt issuance costs	(128)	
Proceeds from issuance of common stock	694	24,226
Proceeds from issuance of convertible secured notes, related party (note 3)	10,560	12,000
Payments of debt obligations		(7,396)
Net cash provided by financing activities	11,125	28,830
Effect of foreign currency exchange rate changes on cash and cash equivalents	57	(61)
Increase in cash and cash equivalents	3,717	8,610
Cash and cash equivalents, beginning of period	6,489	4,874
Cash and cash equivalents, end of period	$ 10,206	$ 13,484

Supplemental cash flow information:		
Cash paid during the period for:		
Income taxes	$ 143	$ 81
Interest	$	$ 12

See accompanying notes to consolidated financial statements

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SIPEX CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

Note 1. Basis of Presentation

Unaudited Interim Financial Information

We have prepared the accompanying 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 Corpor and its wholly-owned subsidiaries, unless the context indicates otherwise. These 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 and nine months ended September 27, 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 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. Such reclassifications had no effect on net loss as previously reported.

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.

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. The Company recorded $5,600 and $50,000 in stock based compensation, reflected in net loss for the three and nine months ended September 27, 2003, respectively. The Company principally grants employee stock options at exercise prices 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: (in thousands, except per share data)

	3 Months Ended		9 Months Ended	
	September 27, 2003	**September 28, 2002**	**September 27, 2003**	**September 28, 2002**
Net loss	$3,345	$21,075	$15,205	$71,525
Less: Total stock-based employee compensation expense determined under fair value based method for all awards, net of related tax effects	4,593	4,109	13,170	11,226

Pro forma net loss	7,938	25,184	28,375	82,751

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		3 Months Ended		9 Months Ended	
		September 27, 2003	September 28, 2002	September 27, 2003	September 28, 2002
Net loss per share:					
Basic and diluted	as reported	$(0.12)	$ (0.75)	$(0.54)	$ (2.66)
Basic and diluted	proforma	$(0.28)	$ (0.90)	$(1.01)	$ (3.07)

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		9 Months Ended	
	September 27, 2003	September 28, 2002	September 27, 2003	September 28, 2002
Average risk-free interest rates	2.1%	4.0%	2.3%	4.0%
Average expected life (in years)	4.0	6.0	4.0	6.0
Volatility	95%	247%	95%	247%

Accounts Receivables Bad Debt Allowance

Accounts receivable allowances for bad debts were approximately $341,000 and $945,000 at September 27, 2003 and December 31, 2002, respectively.

Note 2. Effect of Recent Accounting Pronouncements

In January 2003, the FASB issued FASB Interpretation No. 46, Consolidation of Variable Interest Entities (FIN 46). This interpretation provides guidance on the identification of entities controlled through means other than voting rights. FIN 46 specifies how a business enterprise should evaluate its interests in a variable interest entity to determine whether to consolidate that entity. A variable interest entity must be consolidated by its primary beneficiary if the entity does not effectively disperse risks among the parties involved. A public company with a variable interest in an entity created before February 1, 2003 must apply FIN 46 in the first interim or annual period beginning after June 15, 2003. We do not expect the adoption of FIN 46 to have a material impact on our consolidated financial position, results of operations or cash flows.

In April 2003, the FASB issued SFAS No. 149, Amendment of Statement 133 on Derivative Instruments and Hedging Activities (SFAS 149). SFAS 149 amends and clarifies financial accounting and reporting for derivative instruments, including certain derivative instruments embedded in other contracts and for hedging activities under SFAS No. 133, Accounting for Derivative Instruments and Hedging Activities . SFAS 149 will be effective for contracts entered into or modified after June 30, 2003. The Company adopted SFAS 149 on July 1, 2003. We do not expect the adoption of SFAS 149 to have a material impact on our consolidated financial position, results of operations or cash flows.

On May 15, 2003, the FASB issued SFAS No. 150, Accounting for Certain Financial Instruments with Characteristics of Both Liabilities and Equity (SFAS 150). SFAS 150 requires issuers to classify as liabilities (or assets in some circumstance) three classes of freestanding financial instruments that embody obligations for the issuer. Generally, SFAS 150 is effective for financial instruments entered into or modified after May 31, 2003 and is otherwise effective at the beginning of the first interim period beginning after June 15, 2003. The Company adopted the provisions of SFAS 150 on July 1, 2003. The adoption of SFAS 150 did not have an effect on the Company s consolidated financial statements.

Note 3. Related Party Transactions

As of September 2003, affiliates of Future Electronics, Inc. (Future), our largest distributor, held approximately 8.5 million shares, or approximately 30%, of our outstanding common stock. Future was not a related party in fiscal year 2002.

On September 27, 2002, Sipex sold a convertible secured note (the First Note) with an attached warrant to an affiliate of Future for an aggregate cash amount of $12.0 million. The Company recorded the First Note at $10.4 million and the warrant at $1.6 million (recorded to paid in capital) based upon their estimated fair values at the date of issuance using the Black-Scholes option pricing model. The First Note pays a 5.75% coupon and is convertible after one year into Sipex common stock at a conversion price of $7.50 per share. Following the one year anniversary of the issuance of the First Note, the Company can

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require the conversion of the First Note in installments if for a period of time Sipex common stock trades at a price in excess of 150% of the conversion price of $7.50. The private placement also included a warrant to purchase 900,000 shares of Sipex common stock exercisable for a two-year period beginning on the one-year anniversary of the date of issuance. The exercise price for the warrant is $2.9458. The First Note is secured by a Deed of Trust on the Company s land and building at Milpitas, California.

On June 20, 2003, Sipex sold a convertible secured note (the Second Note) to an affiliate of Future for an aggregate cash amount of approximately $10.6 million. The Second Note pays a 1.5% coupon rate per annum. The principal amount of the Second Note is contingently convertible into a maximum of 3.0 million shares of Sipex common stock at a conversion price of $3.52 per share, subject to Future attaining predetermined annual and/or cumulative sales levels over a three year period. Accordingly, in accordance with EITF 01-01, Accounting for a Convertible Instrument Granted or Issued to a Nonemployee for Goods or Services or a Combination of Goods or Services and Cash , the Company recognized a non cash charge of $1,214,000 against net sales for the fair value of these conversion rights as of September 27, 2003. Such charge was based on Future attaining approximately 19.8% of the predetermined first annual sales target. The fair value of the conversion rights has been measured pursuant to FASB 123, Accounting for Stock-Based Compensation and EITF 96-18, Accounting for Equity Instruments That Are Issued to Other Than Employees for Acquiring, or in Conjunction with Selling, Goods or Services at September 27, 2003. The Second Note is secured by a Deed of Trust on the Company s land and building at Milpitas, California as well as all other assets of the Company, except for the Company s intellectual property.

If the First Note and the Second Note are not converted pursuant to their respective terms, the Company will be required to repay them upon their respective maturity dates. In the event of a default under the terms of the notes, the Company s repayment obligations could be accelerated. In addition, the holder of the Second Note may require early repayment, with a 90 day written demand notice, of $3,000,000 on each of July 31, 2005 and July 31, 2006 and any unpaid amounts due on the Second Note due date of June 30, 2007.

Assuming conversion of the First Note and exercise of the warrant issued in September 2002, entities affiliated with Future would beneficially own approximately 36% of our common stock based on the number of shares outstanding as of September 2003. In addition, if Future attains certain predetermined sales levels over three annual periods, rights to convert the Second Note will vest. If the warrant is exercised and the notes are fully converted to common stock, Future would beneficially own approximately 41% of our common stock based on the number of shares outstanding as of September 2003. However, in connection with the issuance of the June 2003 note, we entered into a standstill agreement with affiliates of Future, pursuant to which these security holders agreed not to acquire more than 35% of our stock on a fully diluted basis.

Also in connection with the issuance of the Second Note, we entered into a voting agreement with an affiliate of Future, pursuant to which this security holder agreed that the additional shares of our common stock issuable upon conversion of the Second Note (i) will not be voted or (ii) will be voted in the same proportion as the votes cast by all other shareholders of Sipex.

Affiliates of Future are not currently represented on our board of directors and do not have contractual rights to such representation or to any participation in the corporate governance or management of the Company.

We have a distributor agreement with Future that provides for Future 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 its inventory of Sipex products. Sipex maintains a separate price list for products sold to Future, which may be different from the prices charged to customers in direct sales transactions. Our distributor agreement with Future does not contain minimum purchase commitments. The Company defers revenue shipments to Future until the product is resold by Future to the end user. These provisions, as well as the significant share ownership by affiliates of Future, cause management to conclude that reasonable estimates of price concessions and returns can not be made at the time of shipment to the distributor.

Future has historically accounted for a significant portion of our revenues. It is our largest distributor worldwide, and accounted for 32.6% of total net sales, prior to taking into account the non cash charge of $1,214,000 for the fair value of the debt conversion rights, for the nine months ended September 27, 2003, and 24%, 21% and 23% of total net sales for the years ended December 31, 2002, 2001 and 2000, respectively. We anticipate that sales of our products to Future will continue to account for a significant portion of our revenues.

Note 4. Net Loss Per Share

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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 represents 3,329,000 and 697,000 potential common shares for the three months ended September 27, 2003 and September 28, 2002, respectively, and 7,495,000 and 2,745,000 potential common shares for the nine months ended September 27, 2003 and September 28, 2002, respectively. Included in the antidilutive potential common share numbers in the preceding sentence and excluded from the dilution calculation were shares issuable upon conversion of the First Note issued to an affiliate of Future, a related party, of 2,184,000 and 692,000 potential common shares for the three months ended September 27, 2003, and September 28, 2002, respectively, and 3,209,000 and 1,885,000 potential common shares for the nine months ended September 27, 2003 and September 28, 2002, respectively.

Note 5. Restructuring

Below is a summary of the activity related to restructuring costs for the nine months ended September 27, 2003.

	Restructuring Costs
Accrual balance December 31, 2002	$ 755
Incurred 2003	
Charges utilized	(426)
Adjustments to accrual	(329)
Accrual balance September 27, 2003	$

During the first nine months of 2003, the Company paid $426,000 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 $329,000 for the reversal of accrued facility exit costs and anticipated severance costs being less than originally expected. No balance existed as of September 27, 2003.

Note 6. Segment Information

The Company s Chief Executive Officer (CEO) is considered to be the Company s chief operating decision maker. The Company has organized its operations based on a single operating segment: the development and delivery of high performance analog integrated circuits that are used primarily by original equipment manufacturers operating in the computing, communications and networking infrastructure markets. The CEO reviews financial information presented on a consolidated basis accompanied by disaggregated information about revenues by product family and geographic region for purposes of making operating decisions and assessing financial performance. We have aligned our organization with the primary management objective of increasing overall sales unit volume, regardless of whether a distributor or the Company is the seller. The disaggregated revenue information reviewed on a product family basis by the CEO includes the optics, interface and power product families along with other legacy product families.

The disaggregated information reviewed on a product basis by the CEO is as follows:

	Three Months Ended		Nine Months Ended	
	September 27, 2003	September 28, 2002	September 27, 2003	September 28, 2002
	(in thousands)			
Net sales				
Optics	$ 2,748	$ 1,099	$ 7,386	$ 1,249
Interface	9,454	8,092	25,279	22,009

Power	4,073	3,398	11,334	11,112
Other (Legacy/EL)	137	4,036	2,420	15,307
Total net sales before fair value of debt conversion rights	$16,412	$16,625	$46,419	$49,677

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The Company markets its products primarily from its operations in the United States. International sales are made primarily to customers in Canada, Europe, Japan and the Pacific Rim. Information regarding the Company s revenues derived from products shipped to different geographic regions is as follows:

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	Three Months Ended		Nine Months Ended	
	September 27, 2003	September 28, 2002	September 27, 2003	September 28, 2002
	(in thousands)			
Net sales				
United States/Canada	$ 3,170	$ 3,436	$10,214	$12,042
Europe	2,701	4,570	7,427	14,705
Japan	4,030	2,220	10,520	3,661
Pacific Rim	6,511	6,399	18,258	19,269
Total net sales before fair value of debt conversion rights	$16,412	$16,625	$46,419	$49,677

The Company s long-lived assets located in countries other than the United States are considered insignificant.

Significant customer information is as follows:

	% of Total Sales Three Months Ended		% of Total Sales Nine Months Ended		% of Total Accounts Receivable,
	September 27, 2003	September 28, 2002	September 27, 2003	September 28, 2002	September 27, 2003
Future	36.1%	27.6%	32.6%	23.7%	27.4%
Microtek, Inc.	21.3%	8.9%	18.8%	4.7%	29.2%
SDV/PC		13.8%		16.4%	

Note 7. Inventories

Inventories consist of (in thousands):

	September 27, 2003	December 31, 2002
Finished Goods	$ 5,871	$ 4,897
Work-in-process	8,953	8,594
Raw Materials	270	902
Total inventory	$15,094	$14,393

Note 8. Accrued Warranty and Other Guarantees

Products are generally sold with a one year warranty. Reserve requirements are recorded in the period of sale and are based on an assessment of the products sold with warranty and historical warranty costs incurred. The Company also assesses its preexisting warranty obligations and may adjust the amounts based on actual experience or changes in future expectations.

The following table summarizes the activity in the warranty reserve for the nine months ended September 27, 2003 (in thousands):

	Warranty Reserve
Accrued warranty, December 31, 2002	$ 69
Cost of warranty claims	(40)
Accruals for warranties during the period	175
Accrued warranty, September 27, 2003	$ 204

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Note 9. Commitments

On August 21, 2003 we announced an exclusive sourcing agreement with PolarFab, a US-based, semiconductor foundry. This arrangement provides us with favorable wafer pricing, delivery and engineering support from PolarFab in return for exclusive manufacturing rights for certain products. We are under obligation to make minimum purchase commitments based on quarterly rolling forecasts extending out one year. We have agreed to purchase no less than 50% of the rolling forecast on an ongoing basis through the term of this agreement. The initial term of the agreement is 5 years with renewals on a negotiated basis.

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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 consolidated financial statements and notes to the consolidated financial statements included in this Form 10-Q, as well as the Management Discussion and Analysis of Financial Condition and Results of Operations and financial statements and notes to the consolidated financial statements 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.

On June 20, 2003, Sipex sold a secured note to an affiliate of Future. The principal amount of this note is contingently convertible up to a maximum of 3.0 million shares of Sipex common stock at a conversion price of $3.52 per share, subject to Future attaining predetermined annual and/or cumulative sales levels over a three year period. During the three month period ended September 27, 2003, Future attained 19.8% of the first year sales target, which resulted in a non cash charge of $1,214,000 against net sales for the fair value of these conversion rights. The Company is seeking to modify the terms of the convertible note or the distribution agreement with Future in order to eliminate, reduce or otherwise mitigate the uncertainties associated with ongoing non cash charges to net sales. However, the Company may be unable to secure such modifications. Additionally, any modifications achieved could result in adverse accounting charges for the period in which such modifications are made.

Critical Accounting Policies

The discussion and analysis of our financial condition and results of operations is based on our 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 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 valuation, 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.

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Revenue recognition

We record revenue to our largest distributor, a related party, when 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 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 and customers. For product sales recognized at the time of shipment, Sipex accrues for estimated future sales returns upon shipment.

We account for the fair value of the debt conversion rights of a convertible note payable to a related party in accordance with Emerging Issues Task Force (EITF 01-1), Accounting for a Convertible Instrument Granted or issued to a Nonemployee for Goods or Services or a Combination of Goods or Services and Cash (See Note 3 to the consolidated financial statements).

Sales returns

To estimate reserves for future sales returns, we regularly review our history of actual returns. 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 customers for which Sipex recognizes revenue upon 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 valuation

We write down inventory for estimated excess quantities, obsolescence or lack of marketability. In addition, we write down inventory to the lower of cost or market. The determination of excess and obsolete inventory 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 plus estimated costs to complete and sell to anticipated market pricing. Inventories are written down when the cost exceeds market which becomes the new cost basis. In establishing inventory valuation, 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, additional inventory write-downs may be required.

Restructuring and impairment

The 2002 restructuring accrual was estimated based on management s plan that included 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. 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 its 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

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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.

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. Our deferred tax assets at September 27, 2003 continue to have a full valuation allowance.

Results of Operations

The table below presents the statements of operations for their respective periods as a percentage of net sales.

	Three Months Ended		Nine Months Ended	
	September 27, 2003	September 28, 2002	September 27, 2003	September 28, 2002
Net sales	100.0%	100.0%	100.0%	100.0%
Cost of sales	76.5	139.5	87.2	112.7
Gross profit (loss)	23.5	(39.5)	12.8	(12.7)
Operating expenses				
Research and development	22.2	20.5	21.5	19.5
Marketing and selling	11.6	10.9	11.3	12.7
General and administrative	10.3	10.9	12.6	12.3
Restructuring and facility exit costs	(0.2)	32.7	(0.7)	10.9
Amortization/impairment of goodwill	0.0	10.9	0.0	9.7
Total operating expenses	43.9	85.9	44.7	65.1
Loss from operations	(20.4)	(125.4)	(31.9)	(77.8)
Total other expense, net	(1.4)	(0.3)	(1.1)	(1.6)
Loss before income taxes	(21.8)	(125.7)	(33.0)	(79.4)

Net Sales

Net sales for the third quarter of 2003 were $15,198,000, impacted by a $1,214,000 non cash charge for the fair value of debt conversion rights in a convertible note payable to a related party (see Note 3). Before considering the impact of this charge, net sales for the third quarter of 2003 were $16.4 million, compared to $16.6 million for the same period in the prior year, or a 1.3% decrease. For the nine months ended September 27, 2003, net sales before the fair value of debt conversion rights decreased 6.6% to $46.4 million, compared to $49.7 million for the same period in the prior year. The $0.2 million decrease in the third quarter of 2003 and the $3.3 million decrease for the nine months ended September 27, 2003, as compared to the corresponding periods last year, were mainly due to the sale of the hybrid and analog display product families to SatCon Electronics Inc. at the end of the third quarter of 2002 and the discontinuance of other legacy product families, accordingly, the Company recognized no net sales for the hybrid and analog display product families in 2003. The decrease in the third quarter of 2003 compared to the same period in 2002 was nearly offset by an increase in the sales of the optics, interface and power product families in the third quarter of 2003. For the third quarter of 2003, net sales from optics, interface and power products increased $1.7 million, $1.4 million and $0.7 million, respectively, compared to the same period last year. For the nine months ended September 27, 2003, the decrease in revenue from the sale of the hybrid and analog product families was partially offset by an increase in sales from the optics and interface product families in the amounts of $6.1 million and $3.3 million, respectively, mostly due to the introduction of additional products within each of these core product families.

Geographically, for the third quarter of 2003 and before the impact of the fair value of debt conversion rights, we experienced sales growth of 81.5% in Japan compared to the same quarter of the prior year, and 187.4% in Japan for the nine months ended September 27, 2003 compared to the same period of 2002. These increases were primarily attributable to the optics product family. Net sales also increased in the Pacific Rim 1.8% in the third quarter of 2003 compared to the same quarter last year, while they decreased 5.2% in the comparable nine month period. Net sales declined 7.7% in the United States/Canada and 40.9% in Europe in the third quarter of 2003, as compared to the third quarter of 2002. For the nine months period ended September 27, 2003 compared to the same period in the prior year net sales declined 15.2% in the United States/Canada and 49.5% in Europe primarily due to sale of the hybrid and analog display product families in the third quarter of 2002.

Gross Profit

Net sales and gross profit for the third quarter and nine months of 2003 were impacted by a $1,214,000 non cash charge for the fair value of debt conversion rights in a convertible note payable to a related party (see Note 3). The impact of this charge was to reduce gross profit as a percentage of net sales for the third quarter of 2003 by 5.6% from 29.1% before the charge to 23.5% after the charge, and for the nine months ended September 27, 2003 by 2.3% from 15.1% to 12.8%. Gross profit after considering the impact of the charge for the third quarter of 2003 increased by $10.1 million compared to the same period last year. For the nine months ended September 27, 2003, gross profit after considering the impact of the charge increased by $12.1 million compared to the same period last year. The improvements in gross margin were primarily due to the benefits realized from restructuring activities and cost reduction efforts along with the introduction of new products offset by write offs of certain non productive manufacturing assets. In addition, during the second quarter of 2002, we recorded an inventory write-off of $1.9 million for the discontinuance of the analog display and hybrid product lines.

Gross margin on related party sales compared to other sales for the three months ended September 27, 2003 was higher due to a richer product mix, including certain new products, and due to the concentration of product sales in North America and Europe.

Research and Development

Research and development expenses for the third quarter of 2003 decreased $30,000 or 0.9%, and for the nine months ended September 27, 2003, research and development expenses increased $58,000, or 0.6%, compared to the same periods in the previous year. For the third quarter of 2003 compared to the third quarter of 2002, research and development costs decreased slightly as increased costs associated with contract designers, impairment of mask sets and depreciation were more than offset by decreased occupancy costs. The slight increase in expenses for the nine months ended September 27, 2003 compared to the same period in 2002 was due to increased headcount and impairment of mask sets, nearly offset by decreased occupancy costs. As a percentage of net sales, research and development increased to 22.2% for the third quarter of 2003, as compared to 20.5% for the same period last year, and for the nine months ended September 27, 2003, as a percentage of net sales, research and development costs increased to 21.5% from 19.5%. These percentage increases were primarily attributable to the foregoing factors as well as the decrease in net sales.

Marketing and Selling

Marketing and selling expenses for the third quarter of 2003 decreased $54,000, or 3.0%, compared to the same quarter in the previous year. For the nine months ended September 27, 2003, marketing and selling expenses decreased $1.2 million, or 18.5%, compared to the same period of the prior year. The decrease in marketing and selling expenses for the third quarter ended September 27, 2003 compared to the same period last year, were due to decreased occupancy, headcount and advertising costs, partially offset by an increase in distributor representative commissions. For the nine month periods, expenses were lower in 2003 mainly due to decreased occupancy, advertising and travel expenses, offset in part by an increase in the Japan sales office spending. As a percentage of net sales, marketing and selling expenses increased to 11.6% for the third quarter of 2003 compared to 10.9% in the same quarter last year primarily due to the decrease in net sales, and decreased to 11.3% for the nine months ended September 27, 2003 compared to 12.7% for the same period of the prior year, primarily due to cost reductions occurring at a faster rate than the decrease in net sales.

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General and Administrative

General and administrative expenses for the third quarter of 2003 decreased $253,000, or 13.9%, compared to the same quarter in the previous year. For the nine months ended September 27, 2003, general and administrative expenses decreased $437,000, or 7.1%, compared to the same period in the previous year. The decreases in the third quarter ended September 27, 2003 compared to the same period last year resulted primarily from reduced costs associated with doubtful accounts and decreased legal fees resulting from lower levels of services, including services related to financing transactions in 2002. For the nine months ended September 27, 2003 compared to the same period last year, the decreased spending resulted from less fund raising activities as well as reductions in staffing levels. These reductions were partially offset by the payment of severance costs in the second quarter of 2003. As a percentage of net sales, general and administrative expenses decreased in the third quarter of 2003 to 9.5% from 10.3% during the same quarter last year as the impact of cost reductions exceeded the impact of the decrease in net sales. As a percentage of net sales general and administrative expenses for the nine months ended September 27, 2003 increased to 12.6% from 12.3% for the comparable period of the prior year primarily due to the decrease in net sales. General and administrative expenses may increase as we expand our financial infrastructure to improve our controls, systems and procedures.

Restructuring Costs, Reorganization, Impairment and Facility Exit Costs

Fiscal 2003

During the third quarter of 2003, the Company made a $50,000 cash severance payment relating to the accrued restructuring liability and reduced the accrual by $29,000 as the Company has completed its obligations relating to the facility exit costs. During the nine months ended September 27, 2003, the Company paid $426,000 on the accrued restructuring balance of $755,000 outstanding as of December 31, 2002. The payments also consisted mainly of employee severance costs. In addition, the accrual was reduced by $329,000 for the reversal of accrued facility exit costs and severance costs being less than originally expected. These payments and adjustments have fully drawn down the original accrual balance of $755,000 from December 31, 2002.

Fiscal 2002

In the third quarter of 2002, Sipex incurred restructuring costs of $5.7 million, an impairment charge of $1.8 million and $1.6 million of reorganization charges. In September 2002, Sipex announced a plan to sell the Company s 4 wafer fabrication facility in San Jose, California and reduce the production output of the 6 wafer fabrication facility in Milpitas, California by moving to a modified five day per week work schedule from the seven day per week operation.

Total third quarter restructuring charges in 2002 related to these actions were $5.7 million, which consisted of $256,000 of severance costs related to an approximate 50 employee reduction in force at both manufacturing facilities, $1.9 million in net write-offs of inventory for the discontinued analog display and hybrid product families, $661,000 of facilities exit costs consisting principally of the remaining lease payments at the San Jose fabrication facility and $2.9 million of fabrication equipment which was written off. The fabrication equipment written off consisted of equipment on the Company s 4 manufacturing product line, which was used mainly in the production of the discontinued analog display wafers and excess equipment on the Company s 6 line.

In addition to the restructuring charges in the third quarter of 2002, an impairment charge of $1.8 million was also incurred for the write down to fair value of the machinery and equipment at the 4 San Jose fabrication facility which was closed by the end of the first quarter of 2003. This sale included a minimum level of royalty payments to be paid annually to the Company for a three year period totaling $400,000. Revenue is recognized as received for these royalties due to the length of time and related uncertainties affecting their ultimate receipt.

During the third quarter of 2002 we also implemented a plan to reorganize the structure of the Company into six functional groups. Changes in management related to this reorganization resulted in a $1.6 million charge for severance and related costs to six former management employees. In the second quarter of 2002, the Company experienced significant changed circumstances resulting from the Company s stock price decreasing during the quarter, which reduced the Company s fair value. These circumstances indicated that the Company s goodwill might not be recoverable. As a result, the Company performed a goodwill impairment test in accordance with SFAS 142. The results of the impairment test indicated that the full amount of the Company s goodwill of $3.0 million was not recoverable and was written off.

Other Expense, Net

Other expense, net was $217,000 in the third quarter of 2003 and $57,000 in the third quarter of 2002. The increase in other expense, net for the third quarter of 2003 compared to the third quarter of 2002 was due to increased interest expense from the

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issuance of the convertible notes issued in the second quarter of 2003 and third quarter of 2002. For the nine months ended September 27, 2003, other expense, net was $481,000 compared to $774,000 for the same period of the prior year. This was mainly due to reduced royalty expenses, currently classified within cost of sales, partially offset by higher interest expense from the convertible note issuance in the third quarter of 2002 and the second quarter of 2003.

Income Taxes

For the third quarter and the nine months ended September 27, 2003, income tax expense consisted of accruals for income taxes relating to our international locations, primarily for our location in Belgium. Income tax expense for the nine months ended September 28, 2002, was the result of providing a full valuation allowance against previously recorded deferred tax assets that were no longer estimated to be recoverable.

Financial Condition, Liquidity and Capital Resources

As of September 27, 2003, we had available funds of $16.7 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 $9.5 million for the nine months ended September 27, 2003 and $10.6 million for the nine months ended September 28, 2002. Net cash used in operating activities in the nine months ended September 27, 2003 resulted primarily from a $15.2 million net loss, of which $7.0 million was non cash related, a $3.2 million increase in accounts receivable, a $0.1 million increase in inventory, a $0.8 million decrease in accrued restructuring charges, and a $0.6 million decrease in accounts payable and accrued expenses, partially offset by an increase in deferred income of $2.6 million and a decrease in prepaid expenses and other current assets of $0.9 million. For the nine months ended September 28, 2002, net cash used in operating activities resulted primarily from a $71.5 million net loss, of which $55.2 million was non-cash related, an $0.8 million increase in accounts receivable, partially offset by an increase of $6.1 million increase in accounts payable and accrued expenses.

Net accounts receivable was $11.1 million and $7.3 million as of September 27, 2003 and December 31, 2002, respectively. The $3.8 million increase was due primarily to increased collections during the fourth quarter of 2002 as well as a higher proportion of sales during the third quarter of 2003 that shipped in the last month of the quarter.

Inventory was $15.1 million and $14.4 million as of September 27, 2003 and December 31, 2002, respectively. The $0.7 million increase in the first nine months of 2003 consisted of an increase in finished goods products.

Net cash provided by (used in) investing activities was $2.1 million and ($9.6 million) for the nine months ended September 27, 2003 and September 28, 2002, respectively. Purchases of property, plant and equipment were $1.4 million for the nine months ended September 27, 2003, and $3.6 million for the nine months ended September 28, 2002. The decrease in property additions for the nine months ended September 27, 2003 compared to September 28, 2002, was due to the ability of the Company to continue to use existing equipment for the expanded sales as opposed to investing in new equipment purchases. Additionally, in the nine months ended September 27, 2003, $3.5 million was provided from the maturity of short-term investment securities, net of purchases.

Net cash provided by financing activities was approximately $11.1 million for the nine months ended September 27, 2003 of which $10.6 million was from the private placement of convertible debt with an affiliate of Future, a distributor for the Company and related party. In the nine months ended September 28, 2002, net cash provided by financing activities was $28.8 million. In the second quarter of 2002, we received cash of $23.5 million, net of placement agent fees and other costs, through the private placement of 3.0 million shares of Sipex common stock. Proceeds from the offering were used to pay down our line-of-credit to zero, with the balance used for general corporate purposes.

We have outstanding convertible secured promissory notes in the approximate amounts of $12.0 million and $10.6 million, plus accrued interest, issued to affiliates of Future in September 2002 and June 2003, respectively. The note holders may convert the notes into our common stock, however, in the case of the 2003 note; the note is not convertible unless Future meets predetermined sales levels as set forth in the note. If the notes are not converted pursuant to their terms, the Company will be required to repay the notes upon their maturity dates. In the event of a default under the terms of the notes, the Company s repayment obligations could be accelerated. In addition, the holder of the 2003 Note may require early repayment of $3,000,000 on each of July 31, 2005 and July 31, 2006. If Sipex is required to repay the notes, the Company may not have sufficient cash available and may be required to obtain alternative sources of financing. Additional financing may not be available or available on terms acceptable to the Company, and could result in additional dilution to existing shareholders.

Our expense levels are based, in part, on expectations of future revenues and are, to a large extent, fixed in the short term. For example, we have a minimum purchase arrangement with one of our suppliers based on requirements forecasted one year in advance. 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.

We believe that our currently available cash, cash equivalents and short-term 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.

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 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.

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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.

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.

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. For example, we have a minimum purchase arrangement with one of our suppliers based on requirements forecasted one year in advance. 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.

In addition, our quarterly and annual operating results may continue to be affected by non cash charges against our net sales for the fair value of conversion rights associated with the note issued to an affiliate of Future, our largest distributor, in June 2003. In this regard, a non cash charge of $1,214,000 for the quarter ended September 27, 2003 reduced our net sales by that amount and increased our net loss by the same amount, adversely impacting our net loss per share. Additional accounting charges related to the note and our relationship with Future may have significant adverse effects on our operating results. Furthermore, if we modify the terms of the convertible note or our distribution agreement with Future in an effort to eliminate, reduce or otherwise mitigate the uncertainties associated with non cash charges, such modifications could result in significant adverse accounting charges for the period in which such modifications are made.

From 2001 through the third quarter of 2003, the semiconductor industry experienced a prolonged and severe downturn that adversely affected our results of operations. Our net sales before the non cash charge for the fair value of debt conversion rights for the quarter ended September 27, 2003 decreased 1.3% from the corresponding prior year period and 1.0% 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.

As a result of the December 31, 2002 audit of the consolidated financial statements, our previous 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 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.

As of September 27, 2003 we had not remedied the material weaknesses in our financial controls, systems and procedures. 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. In this regard, certain key accounting personnel resigned near the end of the third quarter of 2003. While the Company hired temporary replacements and continues to seek permanent replacements, the third quarter end closing process took longer than anticipated and continued to require a significant level of manual reconciliations and adjustments. 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 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 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 85.1% of our net sales in the nine months ended September 27, 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 three or six months shipments (except for Future, 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 until the product is resold by the distributor to the end user (sell-through). These provisions, as well as the significant share ownership by Future, cause management to conclude that reasonable estimates of price concessions and returns cannot be made at the time of shipment to the distributor.

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

Future has historically accounted for a significant portion of our revenues. It is our largest distributor worldwide, and accounted for 32.6% of total net sales before taking into account non cash charges for the fair value of debt conversion rights for the nine months ended September 27, 2003, and 24%, 21% and 23% of total net sales for the years ended December 31, 2002, 2001 and 2000, respectively. We anticipate that sales of our products to Future will continue to account for a significant portion of our revenues. The loss of Future as a distributor, or a significant reduction in orders from Future would materially and adversely affect our operating results, our business, our financial condition and our stock price.

We have a distributor agreement with Future that provides for Future 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, which may be different from the prices charged to customers in direct sales transactions. Our distributor agreement with Future does not contain minimum purchase commitments. As a result, Future could cease purchasing our products with short notice to us. In addition, Future may defer or cancel orders without penalty, which would likely cause our revenues, our business, our financial condition and our stock price to decline.

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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 strategy of marketing products directly to our customers and indirectly through distributors may result in distribution channel conflicts.

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.

Our international sales, excluding Canada, in the nine months period ended September 27, 2003 were $36.2 million or 78% of total net sales before fair value of debt conversion rights and $50.5 million and $44.4 million for the years ended 2002 and 2001, respectively, or 76% and 62% of total net sales before fair value of debt conversion rights, 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 nine months 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

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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.

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 we have. 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 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.

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, and 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.

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. Our employee s are employees at-will, 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.

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

Our Senior Vice President of Finance and Chief Financial Officer, Senior Vice President of Sales and Vice President of Engineering have joined our company in 2003. 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.

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 with the exception of one of our foundries for whom we provide minimum purchase commitments in accordance with our supply agreement announced on August 11, 2003. 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.

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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.

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 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 obtained funding from the private placement of a convertible secured note on June 20, 2003 which provided approximately $10.6 million to the Company, net of costs of issuance.

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We have outstanding convertible secured promissory notes in the approximate amounts of $12.0 million and $10.6 million, plus accrued interest, issued to affiliates of Future in September 2002 and June 2003, respectively. The note holders may convert the notes into our common stock; however, in the case of the 2003 note, the note is not convertible unless Future, a related party, meets certain predetermined sales levels as set forth in the note. If the notes are not converted pursuant to their terms, the Company will be required to repay the notes upon their maturity dates. In the event of a default under the terms of the notes, the Company s repayment obligations could be accelerated. In addition, the holder of the June 2003 Note has the right to cause us to repay a portion of the note early. If the note holder requests such early repayment, we will be required to make payments of $3,000,000 on each of July 31, 2005 and July 31, 2006. If Sipex is required to repay the notes, the Company may not have sufficient cash available and may be required to obtain alternative sources of financing. Additional financing may not be available or available on terms acceptable to the Company, and could result in additional dilution to existing shareholders.

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 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 third quarter of 2003, our stock closing price ranged from a high of $9.29 to a low of $4.68. 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.

We are incurring additional costs and devoting more management resources to comply with increasing regulation of corporate governance and disclosure.

We are spending an increased amount of management time and external resources to understand and comply with changing laws, regulations and standards relating to corporate governance and public disclosure, including the Sarbanes-Oxley Act of 2002, new SEC regulations and Nasdaq Stock Market rules listing requirements. Devoting the necessary resources to comply with evolving corporate governance and public disclosure standards may result in increased general and administrative expenses and a diversion of management time and attention to these compliance activities.

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Affiliates of Future, our largest distributor, beneficially own a significant percentage of our common stock, which will allow them to significantly influence matters requiring shareholder approval and could discourage potential acquisitions of our company.

As of September 2003, affiliates of Future, our largest distributor, held approximately 8.5 million shares of our common stock, or approximately 30%, of our outstanding common stock. Assuming conversion of the promissory note and exercise of the warrant issued to an affiliate of Future in September 2002, Future would beneficially own approximately 36% of our outstanding common stock. In addition, if Future attains certain predetermined sales levels over three annual periods, the right to convert the principal underlying the promissory note issued to an affiliate of Future in June 2003 will vest. If the warrant is exercised and the notes are fully converted to common stock, Future would beneficially own approximately 41% of our common, stock based on the number of shares outstanding as of September 2003. However, in connection with the issuance of the June 2003 note, we entered into a standstill agreement with affiliates of Future, pursuant to which these security holders agreed not to acquire more than 35% of our stock on a fully diluted basis. Also, in connection with the issuance of the June 2003 promissory note, we entered into a voting agreement with an affiliate of Future, pursuant to which this security holder agreed that the additional shares of our common stock issuable upon conversion of the June 2003 note either (i) will not be voted or (ii) will be voted in the same proportion as the votes cast by all other shareholders of Sipex.

Affiliates of Future are not currently represented on our board of directors and do not have contractual rights to such representation or to any participation in the corporate governance of management Sipex. Due to their ownership of a significant percentage of our common stock, these security holders will be able to exert significant influence over actions requiring the approval of our shareholders, including many types of change of control transactions and amendments to our charter documents. The significant ownership percentage of these security holders could have the effect of delaying or preventing a change of control Sipex or otherwise discouraging a potential acquirer from obtaining control of Sipex.

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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.

The Company s exposure to market risk for changes in interest rates relates primarily to the increase or decrease in the amount of interest income the Company can earn on its investment portfolio. The two debt instruments that the Company has entered into have fixed interest rates. We do not use derivative financial instruments or engage in hedging activities in its investment portfolio. We ensure the safety and preservation of its invested principal funds by limiting default risks, market risk and reinvestment risk. The Company mitigates default risk by investing in safe and high-credit quality securities.

At September 27, 2003 we had short-term investments of $6,486,000. Our short-term investments consisted of highly liquid investments with original maturities at the date of purchase of between 91 day and 180 days. These investments are subject to interest rate risk and will fall in value if market interest rates increase. The Company believes a hypothetical increase in market interest rates by 10% from levels at September 27, 2003, would cause the fair value of these short-term investments to fall by an immaterial amount. Since we are not required to sell these investments before maturity, it has the ability to avoid realizing losses on these investments due to a sudden change in market interest rates. On the other hand, declines in the interest rates over time will reduce our interest income.

The Company had two outstanding convertible notes for $21,244,000, at September 27, 2003. These instruments have a fixed interest rate of 1.5% and 5.75% per annum. Because the interest rates of these instruments are fixed, a hypothetical 10% increase in interest rates will not have a material effect on the Company. Interest rate increases, however, will increase interest expense associated with future borrowings by the Company, if any. We do not hedge against interest rate fluctuations.

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Item 4. Controls and Procedures

As of September 27, 2003, 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 were informed by our previous independent auditors as part of the December 31, 2002 audit 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 consolidated financial statements and the lack of proper management review and account analysis. 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. As of September 27, 2003, we had not remedied the material weaknesses in our financial controls, systems and procedures. Certain key accounting personnel resigned near the end of the third quarter of 2003. The Company hired temporary replacements; however, the quarter end closing process took longer than anticipated and continued to require a significant level of manual reconciliations and adjustments.

While the Company hired temporary replacements and continues to seek permanent replacements, the third quarter end closing process took longer than anticipated and continued to require a significant level of manual reconciliations and adjustments.

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

- 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 are implementing improved inventory control systems and procedures throughout our manufacturing lines;
- 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. In this regard we are expanding the finance staff resources to focus on account reconciliations and process improvements.

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 their evaluation and as of the end of the period covered by this quarterly report, 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 control over financial reporting that occurred during our last fiscal quarter that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

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Part II: OTHER INFORMATION

Item 1. Legal Proceedings

None.

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.

Item 5. Other Information

On July 10, 2003, the Company filed an 8-K naming Deloitte and Touche LLP as the Company s new independent auditors.

On October 28, 2003, the Company filed a Form 8-A with Securities and Exchange Commission announcing it completed its reincorporation from the Commonwealth of Massachusetts to the State of Delaware and amended its By Laws.

Item 6. Exhibits and Reports on Form 8-K

(a) Exhibits

Exhibit Number	Title
31.1	Certification of CEO pursuant to Section 302 the Sarbanes-Oxley Act of 2002.
31.2	Certification of CFO pursuant to Section 302 the Sarbanes-Oxley Act of 2002.
32.1	Certification of CEO pursuant to Section 906 the Sarbanes-Oxley Act of 2002.
32.2	Certification of CFO pursuant to Section 906 the Sarbanes-Oxley Act of 2002.

(b) Reports on Form 8-K

We filed or furnished four reports on Form 8-K during the quarter ended September 27, 2003. Information regarding each item reported on is as follows:

Date filed or furnished	Item No.	Description
July 10, 2003	4	On July 10, 2003 the Company named Deloitte and Touche LLP as the Company s new independent auditors.
July 25, 2003	7 and 9	On July 23, 2003 the Company issued a press release announcing preliminary revenue results for the fiscal quarter ended June 28, 2003.
August 5, 2003	7 and 12	

		On August 4, 2003 the Company issued a press release announcing results for the fiscal quarter ended June 28, 2003.
August 7, 2003	7 and 12	On August 4, 2003 the Company filed a form 8-K with the transcript of conference call of August 4, 2003 relating to Sipex Corporation s results for the fiscal quarter ended June 28, 2003.

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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: November 17, 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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Exhibit Index

Exhibit Number	Title
31.1	Certification of CEO pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification of CFO pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Certification of CEO pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2	Certification of CFO pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.