

U.S. SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, DC 20549

FORM 10-QSB

(Mark One)

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

For the quarterly period ended September 30, 2001

- --- 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: 001-13467

COMMONWEALTH BIOTECHNOLOGIES, INC.

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

Virginia  
(State or other jurisdiction  
of incorporation or organization)

54-1641133  
(I.R.S. Employer  
Identification No.)

601 Biotech Drive, Richmond, Virginia 23235  
(Address of principal executive offices)

(804) 648-3820  
(Issuer's telephone number)

-----

Check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act 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  
--- ---

As of November 13, 2001, 2,076,164 shares of common stock, no par value, of the registrant were outstanding.

Transitional Small Business Disclosure Format (Check one) Yes: No: X  
--- ---

Commonwealth Biotechnologies, Inc.

INDEX

	Page Number -----
PART I. FINANCIAL INFORMATION	
Condensed Consolidated Balance Sheets September 30, 2001 and December 31, 2000	3
Condensed Consolidated Statements of Operations, Three Months and Nine Months Ended September 30, 2001 and 2000	4
Condensed Consolidated Statements of Cash Flows, Nine Months Ended September 30, 2001 and 2000	5
Notes To Consolidated Financial Statements	6
Management's Discussion and Analysis	8
PART II. OTHER INFORMATION	17
SIGNATURES	18

<TABLE>  
<CAPTION>

December 31, 2000	September 30, 2001	
	(Unaudited)	<C>
Assets		
Current Assets		
Cash and cash equivalents	\$ 151,990	\$
587,156		
Accounts receivable	783,153	
792,071		
Investments	--	
995,789		
Prepaid expenses and inventory	275,389	
94,866		
-----		
Total current assets	1,210,532	
2,469,882		
-----		
Property and Equipment, net	6,995,943	
7,153,852		
-----		
Other Assets		
Restricted cash	466,632	
445,020		
Bond issue costs, net	230,635	
238,693		
Contract acquisition costs	45,762	
33,047		
Deposits	--	
3,200		
-----		
Total other assets	743,029	
719,960		
-----		
	\$ 8,949,504	\$
10,343,694	=====	
-----		
Liabilities and Stockholders' Equity		
Current Liabilities		
Demand note payable	\$ 94,679	\$
134,680		
Current maturities of long term debt and capital lease	195,679	
207,431		
Accounts payable and other current liabilities	413,881	
548,914		
Deferred revenue	23,659	
25,718		
-----		
Total current liabilities	727,898	
916,743		
-----		
Long Term Debt		
-----		
Bonds payable	8,825,000	
3,915,000		
Capital lease	88,607	
162,386		
-----		
Total long term debt	3,913,607	
4,077,386		
-----		
Stockholders' Equity		
Common stock, no par value, 10,000,000 shares authorized	--	

--  
September 30, 2001- 2,076,164; December 31, 2000 - 2,076,164 shares issued and  
outstanding  
Additional paid-in capital 11,893,939  
11,905,864  
Accumulated deficit (7,585,940)  
(6,565,155)  
Accumulated other comprehensive income --  
8,856

-----  
Total stockholders' equity 4,307,999  
5,349,565  
-----

10,343,694 \$ 8,949,504 \$  
=====

</TABLE>

See notes to financial statements.

Commonwealth Biotechnologies, Inc.  
Statements of Operations

<TABLE>  
<CAPTION>

	Three Months Ended		Nine Months Ended	
	September 30, 2001	September 30, 2000	September 30, 2001	September 30, 2000
	(Unaudited)		(Unaudited)	
	<C>	<C>	<C>	<C>
Revenue				
Lab Services	\$ 242,741	\$ 297,189	\$ 530,608	\$ 695,569
Commercial contracts	398,893	158,243	1,490,837	925,268
Government contracts	240,664	454,406	1,106,809	1,499,176
Food safety / microbiology	7,964	--	10,464	--
Genetic identity	52,420	86,576	185,962	181,159
Clinical services	58,554	--	95,359	--
License fees	--	--	400,000	--
Product sales	2,137	3,010	8,677	8,800
Other revenue	1,310	209	5,294	787
Total revenue	1,004,683	999,633	3,834,010	3,310,759
Costs of services				
Direct Labor	252,474	216,122	897,738	685,599
Direct Materials	120,202	115,010	470,071	366,353
Subcontractor Costs	2,500	5,590	101,922	16,230
Overhead	500,101	450,211	1,557,514	1,198,338
Total costs of services	875,277	786,933	3,027,245	2,266,520
Gross Profit	129,406	212,700	806,765	1,044,239
Selling, General & Administrative	469,785	442,993	1,687,859	1,116,441
Operating income (loss)	(340,379)	(230,293)	(881,094)	(72,202)
Other income (expenses)				
Interest expense	(69,632)	(86,152)	(212,933)	(252,994)
Interest income	9,874	8,087	73,242	25,748
Total other income (expense)	(59,758)	(78,065)	(139,691)	(227,246)
Net loss	\$ (400,137)	\$ (308,358)	\$ (1,020,785)	\$ (299,448)
Diluted loss per common share	(0.19)	(0.18)	(0.49)	(0.17)

</TABLE>

See notes to financial statements.

Commonwealth Biotechnologies, Inc.  
Statements of Cash Flows

<TABLE>  
<CAPTION>

	Nine Months Ended	
	September 30, 2001	September 30, 2000
	(Unaudited)	
<S>	<C>	<C>
<b>Cash Flows from Operating Activities</b>		
Net loss	\$(1,020,785)	\$ (299,448)
Adjustments to reconcile net loss to net cash used in operating activities		
Depreciation and amortization	635,448	449,784
Realized gains on sale of investments	(20,565)	--
Non-cash license fee	(200,000)	--
Changes in:		
Accounts receivable	208,918	(317,888)
Prepaid expenses and inventory	(180,524)	(64,410)
Accounts payable and accrued expenses	(135,033)	(82,926)
Deposits	3,200	--
Deferred revenue	(2,059)	(74,035)
<b>Net cash used in operating activities</b>	<b>(711,400)</b>	<b>(240,853)</b>
<b>Cash Flows from Investing Activities</b>		
Contract acquisition costs	(150,000)	--
Purchase of debt securities for sale	(296,889)	--
Sale of debt securities for sale	1,305,204	--
Purchases of property, plant and equipment	(333,013)	(210,466)
<b>Net cash provided by (used in) investing activities</b>	<b>525,302</b>	<b>(210,466)</b>
<b>Cash Flows from Financing Activities</b>		
Issuance of common stock	(11,925)	2,987,528
Principal payments on debt	(215,531)	(415,532)
Restricted cash	(21,612)	(16,560)
<b>Net cash provided by (used in) financing activities</b>	<b>(249,068)</b>	<b>2,555,436</b>
<b>Net increase (decrease) in cash and cash equivalents</b>	<b>(435,166)</b>	<b>2,104,117</b>
<b>Cash and cash equivalents, beginning of period</b>	<b>\$ 587,156</b>	<b>\$ 31,630</b>
<b>Cash and cash equivalents, end of year</b>	<b>\$ 151,990</b>	<b>\$ 2,135,747</b>
<b>Supplemental Disclosure of Cash Flow Information</b>		
Cash payments for interest	\$ 204,875	\$ 226,865
<b>Supplemental schedule of non-cash investing and financing activities</b>		
Capital lease obligation incurred for use of equipment	\$ --	\$ 378,825

</TABLE>

See notes to financial statements.

Commonwealth Biotechnologies, Inc.  
Notes To Financial Statements

Note 1. Basis of Presentation

The accompanying unaudited financial statements (except for the balance sheet at December 31, 2000, which is derived from audited financial statements) have been prepared in accordance with generally accepted accounting principles for interim financial statements and Regulation S-B. Accordingly, they do not include all of the information required by generally accepted accounting principles for complete financial statements. In the opinion of the Company, all adjustments (consisting of only normal recurring accruals) necessary to present fairly the financial position and the results of operations for the periods presented have been included. The results of operations for the three and nine months ended September 30, 2001 are not necessarily indicative of the results that may be expected for the year ending December 31, 2001.

## Note 2. Earnings (Loss) Per Share

The Company follows the guidance provided in SFAS 128, Earnings Per Share, which establishes standards for computing and presenting earnings per share and applies to entities with publicly held common stock or potential common stock. Those entities that have only common stock outstanding are required to present only basic per share amounts. Diluted per share amounts assume the conversion, exercise or issuance of all potential common stock instruments such as warrants and convertible securities, unless the effect is to reduce a loss or increase earnings per share. At September 30, 2001 and 2000, the Company had stock options and warrants outstanding that were anti-dilutive since the Company incurred a net loss for all periods presented.

## Note 3. Contract Purchase

On January 1, 2001, the Company purchased contracts and rights to pending contracts held by the drug development group of SRA Life Sciences, Inc. of Falls Church, Virginia for \$150,000. In connection with this purchase, the Company incurred acquisition costs, during 2000, totaling \$33,047. These costs have been capitalized and will be amortized over the life of the contracts which all expire in 2001.

## Note 4. Patent Agreement

On April 30, 2001 the Company signed a patent license agreement (U.S. Patent No. 6,110,683 entitled "Automated DNA Sequencer Loading Dye Which Contains A Lane Tracking Aid issued August 29, 2000) with Applied Biosystems Group of PE

6

Corporation, New York. This license agreement grants Applied Biosystems a non-exclusive, worldwide, perpetual, non-assignable license under the Patent. This enables them to research, develop, make, have made, import, market, use, sell, have sold, offer to sale, distribute, have distributed and otherwise exploit products and services and to pass on to end user customers of Applied Biosystems or its distributors the right to use such product and services. The Company received licensing fees of \$400,000 of which \$200,000 was received in cash in the second quarter and the remaining \$200,000 in product and service credits. With the credits received from the license agreement, the Company purchased equipment, which was placed in service in the third quarter.

## Note 5. Business Considerations

Since 1997 and through 2001, the Company has incurred recurring operating losses due to increased operating costs without corresponding increases in revenues. Through September 30, 2001, these deficits along with capital needs were substantially funded through use of funds obtained from the following:

- o In June 1997, the Company completed an initial public offering (IPO) whereby they received proceeds of \$2,626,269, net underwriting and other offering costs.
- o In March 1998, the Company sold Industrial Revenue Development Bonds totaling \$4,000,000.
- o In September 2000, the Company completed a private placement of 348,000 shares of common stock. Net proceeds to the Company from this private placement amounted to \$2,350,397.

The Company realizes that in order for it to continue its operations, it must take steps in achieving a positive cash flow. Management is taking the following steps targeted to resolve this issue:

- 1) reduction of management salaries,
- 2) elimination of non-essential positions,
- 3) aggressive budget reduction in operating expenses,
- 4) increased management focus in obtaining additional revenue,
- 5) actively seeking additional private equity and or debt financing.

It is the intention of the Company throughout the next twelve months to become cash positive and make a profit. By increasing revenues and implementing aggressive cost cutting measures, Management believes that the Company can attain both objectives.

## Note 6. Comprehensive Income

Comprehensive income (loss) as of the three and nine months ended September 30, 2001 is \$(400,137) and \$(1,010,178), respectively. Comprehensive income (loss) for the three months and nine months ended September 30, 2000 consisted only of net income (loss).

7

The following should be read in conjunction with the Company's Financial Statements and Notes included herein.

Business Considerations (see note # 5)

#### Overview

The Company's revenues are derived principally from providing macromolecular synthetic and analytical services to researchers in the biotechnology industry or who are engaged in life sciences research in government or academic labs throughout the world. Development of innovative technologies for biotechnology requires sophisticated laboratory techniques and the Company provides these services to customers on a contract basis. The Company's customers consist of private companies, academic institutions and government agencies, all of which use biological processes to develop products for health care, agricultural, and other purposes.

The Company generally derives revenue from two types of customers: those who require a discrete set of services ("lab services"), and those who contract with the Company on an extended basis for performance of a variety of integrated services ("commercial, drug development and government contracts"). More often than not, the Company's customers provide repeat business to the Company. The Company views commercial, drug development and government contracts as the more important source of revenue. The Company has continued to focus its efforts on identifying these customers. These contracts generally range from a few months to more than a year. Revenues are generally recognized as services are rendered or as products are delivered. In addition, revenue is also recognized with performance-based installments payable over the contract duration as milestones are achieved.

The Company also derives revenues from genetic identity and clinical services. There has been a dramatic and constant increase in the number of private paternity cases implemented at the Company. The Company routinely processes upwards of 125 inquiries per month. The Company implemented rapid and novel techniques for genotyping analysis that have been applied to cell culture lines. The Company now performs identity and lineage analysis on different cell lines for various clients.

The Company realized a loss from operations for the nine months ended September

8

30, 2001 of \$1,020,785. This deficit resulted because certain new and existing contracts did not produce expected revenues as they were either postponed to subsequent periods or did not materialize.

#### Results of Operations

Three Months Ended September 30, 2001 Compared with Three Months Ended September 30, 2000.

The Company experiences fluctuations in all revenue categories. Continuation of existing projects, or engagement for future projects is usually dependent upon the customer's satisfaction with the scientific results provided in initial phases of the scientific program. Continuation of existing projects or engagement of future projects also often depends upon factors beyond the Company's control, such as the timing of product development and commercialization programs of the Company's customers. The combined impact of commencement and termination of research contracts from several large customers and unpredictable fluctuations in revenue for laboratory services can result in very large fluctuations in financial performance.

#### Revenues

Gross revenues increased by \$5,050 or .5% from \$999,633 during the third quarter of 2000 (the "2000 Quarter") to \$1,004,683 during third quarter of 2001 (the "2001 Quarter").

Revenues realized from lab services decreased by \$54,448 or 18.3% from \$297,189 during the 2000 Quarter to \$242,741 during the 2001 Quarter. Even with management's decision to focus on commercial and government projects, the Company continues to view lab services as a potential revenue source. Historically, net revenues have been earned from lab services, however, the Company views commercial and government projects as the more important source of revenue (as mentioned below) and has continued to focus its efforts on identifying long-term customers.

Revenues realized from various commercial contracts increased by \$240,650 or 152.1%, from \$158,243 during the 2000 Quarter to \$398,893 during the 2001 Quarter. This increase is primarily due to work being done on forty-five individual projects currently in progress. Of the \$398,893 in commercial contracts, revenues earned from the quarter were not associated with any one

major client.

Revenues realized from various government contracts decreased by \$213,742 or 47.0%, from \$454,406 during the 2000 Quarter to \$240,664 during the 2001 Quarter. This category primarily consists of the project that was awarded from the Illinois Institute of Technology Research Institute (see "Business Considerations"). During the

9

third Quarter of 2000, the second year of this contract was awarded to the Company. Third quarter revenues amounted to \$58,000. The reduction in revenue was primarily due to the completion of the second year of the project prior to the start of the third quarter. The Company expects that the third year of the project will be awarded with expected revenues of \$790,000.

Revenues realized from genetic identity decreased by \$34,156 or 39.4%, from \$86,576 during the 2000 Quarter to \$52,420 during the 2001 Quarter. This decrease is a direct result from one of our clients performing the work internally.

In 2001, the Company implemented rapid and novel techniques for genotyping analysis that have been applied to cell culture lines. Consequently, the company performs identity and lineage analysis on different cell lines for various clients. Total revenue derived from genotyping services alone amounted to \$58,554 during the 2001 Quarter.

#### Cost of Services

Cost of services consists primarily of materials, labor, subcontractor costs and overhead. The cost of services increased by \$88,344 or 11.2%, from \$786,933 during the 2000 Quarter to \$875,277 during 2001 Quarter. The cost of services as a percentage of revenue was 87.1% and 78.7% during the 2001 and 2000 quarters, respectively.

Labor costs increased by \$36,352, or 16.8%, from \$216,122 during the 2000 Quarter to \$252,474 during the 2001 Quarter. This increase reflects additional hours being directly charged to projects.

The costs for direct materials increased by \$5,192, or 4.5%, from \$115,010 during the 2000 Quarter, to \$120,202 during the 2001 Quarter. These costs are directly attributable to the revenue generated by the Company.

Overhead cost consists of indirect labor, depreciation, freight charges, repairs and miscellaneous supplies not directly related to a particular project. Total overhead costs increased by \$49,890, or 11.1%, from \$450,211 during the 2000 Quarter to \$500,101 during the 2001 Quarter. This increase is primarily due to amortization costs in the amount of \$45,761 from Drug Development contracts purchased in January 2001.

#### Sales, General and Administrative

Sales, general and administrative expenses ("SGA") consist primarily of compensation and related costs for administrative, marketing and sales personnel, facility expenditures, professional fees, consulting, taxes, and depreciation. Total SGA costs increased by \$26,792, or 6.0%, from \$442,993 during the 2000 Quarter to \$469,785 during 2001 Quarter. As a percentage of revenue, these costs were 46.7% and 44.3%

10

during 2001 and 2000, respectively.

Total compensation and benefits increased by \$25,284 or 17.8% from \$141,763 during the 2000 Quarter to \$167,047 during the 2001 Quarter. This increase is primarily attributable to the reallocation of personnel that were once charged to work on the subcontract from the Illinois Institute of Technology Research Institute back to the administrative area. In addition, three employees were added to assist in the administrative support of the Company. Professional fees decreased by \$25,462, or 28.0%, from \$90,873 during the 2000 Quarter to \$65,411 during the 2001 Quarter. This decrease is primarily due to legal costs associated with patent costs not occurring in the 2001 quarter. Office Expenses decreased by \$30,371, or 66.8% from \$45,415 during the 2000 Quarter to \$15,044 during the 2001 Quarter. This reduction is a direct result of eliminating various items previously purchased in prior periods not needed by the Company. Marketing costs increased by \$41,688 or 117.9%, from \$35,351 during the 2000 Quarter to \$77,039 during the 2001 Quarter. During the third quarter of 2001, the Company continued to increase its marketing exposure throughout the marketplace with major increases in advertising and public relations.

#### Other Income (Expenses)

Interest income increased by \$1,787, or 22.1% from \$8,087 during the 2000

Quarter to \$9,874 during the 2001 Quarter. Interest income has been derived from investing the unused portion of the restricted cash realized by the Company from the successful sale (March 1998) of Industrial Revenue Bonds (IRBs) for construction of the Company's new facility. Interest income also increased due to the investing of the proceeds received from the private placement on September 27, 2000.

Interest costs incurred by the Company during the 2000 and 2001 Quarters included 1) interest paid to financial institutions for loans made to the Company; 2) interest paid for the Company's IRBs; and 3) amortization of costs incurred as a consequence of the completion of the Company's IRB financing. Interest expense and amortization decreased \$16,520 or 19.10% from \$86,152 during the 2000 Quarter to \$69,632 during the 2001 Quarter. This decrease is the result of payments on the principal balance of long-term debt.

#### Results of Operations

Nine Months Ended September 30, 2001 Compared with Nine Months Ended September 30, 2000.

#### Revenues

Gross revenues increased by \$523,251 or 15.8% from \$3,310,759 during the 2000 Period ("the 2000 Period") to \$3,834,010 during the 2001 Period. ("the 2001 Period").

Revenues realized from lab services decreased by \$164,961 or 23.7% from \$695,569

11

during the 2000 Period to \$530,608 during the 2001 Period. As mentioned in the results of operations for the quarter, the Company continues to view lab services as a potential revenue source. However, the Company views commercial and government projects as the more important source of revenue (as mentioned below) and has continued to focus its efforts on identifying long-term customers.

Revenues realized from various commercial contracts increased by \$565,569 or 61.1%, from \$925,268 during the 2000 Period to \$1,490,837 during the 2001 Period. This increase is primarily due to work on ninety-three projects that have either been completed or are in the process being done. Of the \$1,490,837 in commercial contracts one major client represents 11.6% of the revenue earned during the 2001 Period.

Revenues realized from various government contracts decreased by \$392,367 or 26.1%, from \$1,499,176 during the 2000 Period to \$1,106,809 during the 2001 Period. As mentioned in the results from operations for the quarter, this category primarily consists of the project that was awarded from the Illinois Institute of Technology Research Institute (see "Business Considerations"). During the third Quarter of 2000, the second year of this contract was awarded to the Company and provided revenues of approximately \$1.2 million. This revenue was recognized during the last three months of 2000 and the first six months of 2001. The Company expects that the third year of the project will be awarded with expected revenues of \$790,000.

In 2001, the Company implemented rapid and novel techniques for genotyping analysis that have been applied to cell culture lines. Consequently, the company performs identity and lineage analysis on different cell lines for various clients. Total revenue derived from genotyping services alone amounted to \$95,359 during the 2001 Period.

On April 30, 2001 the Company executed a patent license agreement (U.S. Patent No. 6,110,683) with Applied Biosystems Group of PE Corporation, New York. The Company received licensing fees of \$400,000 of which \$200,000 was received in cash in the second quarter and the remaining \$200,000 in product and service credits.

#### Cost of Services

Cost of services consists primarily of materials, labor, subcontractor costs and overhead. The cost of services increased by \$760,725 or 33.5%, from \$2,266,520 during the 2000 Period to \$3,027,245 during 2001 Period. The cost of services as a percentage of revenue was 78.9% and 68.4% during the 2001 and 2000 Periods, respectively. This percentage increase was primarily due to additional expenditures in subcontractor costs (see below.)

Labor costs increased by \$212,139, or 30.9%, from \$685,599 during the 2000 Period to \$897,738 during the 2001 Period. This increase reflects additional hours being directly charged to projects.

12

The costs for direct materials increased by \$103,718, or 28.3%, from \$366,353

during the 2000 Period, to \$470,071 during the 2001 Period. These increased costs are directly attributable to the increase of revenue generated by the Company.

Subcontractor costs increased by \$85,692, or 527.9%, from \$16,230 during the 2000 Period to \$101,922 during the 2001 Period. This increase is due to costs incurred from subcontractors in the new drug development activity that was placed in operation in the 2001 Period.

Overhead cost consists of indirect labor, depreciation, freight charges, repairs and miscellaneous supplies not directly related to a particular project. Total overhead costs increased by \$359,176 or 29.9%, from \$1,198,338 during the 2000 Period to \$1,557,514 during the 2001 Period. This increase is primarily due to the following: 1) indirect labor, \$81,564, 2) fringe benefits from increased costs and additional personnel, \$52,423 3) amortization costs of \$137,285 from the acquisition of the Drug Development contracts in January 2001, 4) increased depreciation expense, \$52,298, 5) and general supplies not directly associated with any particular project also contributed to this increase by \$66,275.

#### Sales, General and Administrative

Sales, general and administrative expenses ("SGA") consist primarily of compensation and related costs for administrative, marketing and sales personnel, facility expenditures, professional fees, consulting, taxes, and depreciation. Total SGA costs increased by \$571,418, or 51.1%, from \$1,116,441 during the 2000 Period to \$1,687,859 during 2001 Period. As a percentage of revenue, these costs were 44.0% and 33.7% during 2001 and 2000, respectively.

Total compensation and benefits increased by \$236,106 or 84.1% from \$280,546 during the 2000 Period to \$516,652 during the 2001 Period. As mentioned in the results from operations for the quarter, this increase is primarily attributable to the reallocation of personnel that were once charged to work on the subcontract from the Illinois Institute of Technology Research Institute back to the administrative area. In addition, three employees were added to assist in the administrative support of the Company. Facility costs increased by \$54,784 or 37.1% from \$147,657 during the 2000 Period to \$202,441 during the 2001 Period. This increase is primarily due to rent paid for the offices of the drug development group. Maintenance and repairs increased by \$25,319, or 195.7%, from \$12,936 during the 2000 Period to \$38,255 during the 2001 Period. This increase is primarily due additional operating leased equipment needed to support the offices of the drug development group. Professional fees increased by \$67,010, or 28.9%, from \$231,766 during the 2000 Period to \$298,776 during the 2001 Period. This increase is primarily due to consulting fees incurred to insure the continuation of a smooth transition of the drug development offices. In addition, the Company opted to increase its coverage in personal liability for both the corporate and drug development offices. Total taxes and licenses increased by \$20,557 or 27.2% from \$75,392 during the 2000 Period to \$95,949 during the 2001 Period. This increase is due to additional

13

sales tax being paid to the Virginia Department of Taxation on various products purchased by the Company. Office Expenses decreased by \$25,430, or 23.0% from \$110,092 during the 2000 Period to \$84,662 during the 2001 Period. This reduction is a direct result of eliminating various items previously purchased in prior periods not needed by the Company. Marketing Expenses increased by \$208,547, or 238.8% from \$87,331 during the 2000 Period to \$295,878 during the 2001 Period. During the 2001 Period, the Company opted to increase its marketing exposure with major increases in advertising and public relations.

#### Other Income (Expenses)

Interest income increased by \$47,494, or 184.4% from \$25,748 during the 2000 Period to \$73,242 during the 2001 Period. Interest income has been derived from investing the unused portion of the restricted cash realized by the Company from the successful sale (March 1998) of Industrial Revenue Bonds (IRBs) for construction of the Company's new facility. Interest income also increased due to the investing of the proceeds received from the private placement on September 27, 2000.

Interest costs incurred by the Company during the 2000 and 2001 Periods included 1) interest paid to financial institutions for loans made to the Company; 2) interest paid for the Company's IRBs; and 3) amortization of costs incurred as a consequence of the completion of the Company's IRB financing. Interest expense decreased \$40,061 or 15.8% from \$252,994 during the 2000 Period to \$212,933 during the 2001 Period. This decrease is the result of payments on the principal balance of long-term debt.

#### Liquidity and Capital Resources

##### Business Considerations (see note # 5)

The 2001 Period reflected a decrease in cash of \$711,400 from operating activities, as compared to a decrease of \$240,853 from operating activities

during the 2000 Period. The significant cash outflow for 2001 was primarily due to substantial investments made by the Company in facility costs, personnel, equipment, sales, and marketing efforts. The cost outlays in 2001 were made possible by capital realized from the Company's private placement on September 27, 2000.

Net working capital as of September 30, 2001 and December 31, 2000 was \$482,634 and \$1,553,139 respectively. This decrease is a direct result of the significant loss in the 2001 Period of \$1,020,785. Cash flows from new and existing contracts that were expected to occur in the first quarter either were postponed to subsequent periods or did not materialize. As a result management is seeking sources of new capital which it believes will be necessary to fund future operations.

On April 30, 2001 the Company signed a patent license agreement (U.S. Patent No. 6,110,683 entitled "Automated DNA Sequencer Loading Dye Which Contains A Lane

14

Tracking Aid issued August 29, 2000) with Applied Biosystems Group of PE Corporation, New York. This license agreement grants Applied Biosystems a non-exclusive, worldwide, perpetual, non-assignable license under the Patent. This enables them to research, develop, make, have made, import, market, use, sell, have sold, offer to sale, distribute, have distributed and otherwise exploit products and services and to pass on to end user customers of Applied Biosystems or its distributors the right to use such product and services. The Company received licensing fees of \$400,000 of which \$200,000 was received in cash in the second quarter and the remaining \$200,000 in product and service credits. These credits were utilized in the third quarter.

The Company continues to search for long-term projects as the more important source of revenue and has continued to focus its efforts on identifying long-term customers. Long-term projects generally range from a few months to more than a year. In the fourth quarter of 1999, the Company was awarded a five-year subcontract with the Illinois Institute of Technology Research Institute. The contract is valued at approximately \$8.5 million. During the third Quarter of 2000, the second year of this contract was awarded to the Company and provided revenues of approximately \$1.2 million. This revenue was recognized during the last three months of 2000 and the first nine months of 2001. The Company expects that the third year of the project will be awarded with expected revenues of \$790,000.

Management has in the past and will continue to seek additional equity and or debt financing in the future to further the Company's development.

#### Forward Looking Statements

Management has included herein certain forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. When used, statements that are not historical in nature, including the words "anticipated", "estimate", "should", "expect", "believe", "intend", and similar expressions are intended to identify forward-looking statements. Such statements are, by their nature, subject to certain risks and uncertainties.

Among the factors that could cause the actual results to differ materially from those projected are the following:

- o business conditions and the general economy,
- o the development and implementation of the Company's long-term business goals,
- o federal, state, and local regulatory environment,
- o lack of demand for the Company's services,

15

- o the ability of the Company's customers to perform services similar to those offered by the Company "in-house,"
- o potential cost containment by the Company's customers resulting in fewer research and development projects,
- o the Company's ability to receive accreditation to provide various services, including, but not limited to paternity testing, and
- o the Company's ability to hire and retain highly skilled employees,

Other risks, uncertainties, and factors that could cause actual results to differ materially from those projected are detailed from time to time in reports filed by the company with the Securities and Exchange Commission, including

PART II  
OTHER INFORMATION

## Item 1. Legal Proceedings

Not applicable.

## Item 2. Changes in Securities and Use of Proceeds

Not applicable.

## Item 3. Defaults Upon Senior Securities

Not applicable.

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

Not applicable.

## Item 5. Other Information

Not applicable.

## Item 6. Exhibits and Reports on Form 8-K

## (a) Exhibits.

Exhibit Number	Description of Exhibit
3.1	Amended and Restated Articles of Incorporation (1)
3.2	Amended and Restated Bylaws (1)
4.1	Form of Common Stock Certificate (1)
4.2	Indenture of Trust by and between the Virginia Small Business Financing Authority and Crestar Bank relating to

17

	the issuance of industrial revenue bonds for the benefit of the Company (2)
10.1	Warrant Agreement between the Company and Richard J. Freer, as amended (1)
10.2	Warrant Agreement between the Company and Thomas R. Reynolds, as amended (1)
10.3	Warrant Agreement between the Company and Robert B. Harris, as amended (1)
10.4	Employment Agreement for Richard J. Freer (1)
10.5	Employment Agreement for Thomas R. Reynolds (1)
10.6	Employment Agreement for Robert B. Harris (1)
10.7	Executive Severance Agreement for Richard J. Freer (1)
10.8	Executive Severance Agreement for Thomas R. Reynolds (1)
10.9	Executive Severance Agreement for Robert B. Harris (1)
10.10	1997 Stock Incentive Plan, as amended (1)
10.11	Loan Agreement by and between the Virginia Small Business Financing Authority and the Company (2)

- 
- (1) Incorporated by reference to the Company's Registration Statement on Form SB-2, Registration No. 333-31731, as amended.
- (2) Incorporated by reference to the Company's Current Report on Form 8-K, dated April 6, 1998, File No. 001-13467.

- (b) Reports on Form 8-K. No reports on Form 8-K were filed for the period covered by this report.

## SIGNATURES

In accordance with the requirements of the Exchange Act, the registrant caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

By: /s/ James H. Brennan

-----  
James H. Brennan  
Controller and Principal Accounting  
Officer

November 13, 2001