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IGI INC
Form 10-Q
November 12, 2004

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, DC 20549

Form 10-Q

(Mark One)

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

For the quarterly period ended September 30, 2004 or

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

For the transition period from _____ to _____

Commission File Number 001-08568

IGI, Inc.

(Exact name of registrant as specified in its charter)

Delaware
(State or other Jurisdiction of
incorporation or organization)

01-0355758
(I.R.S. Employer
Identification No.)

105 Lincoln Avenue
Buena, New Jersey
(Address of Principal Executive Offices)

08310
(Zip Code)

(856) 697-1441
(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15 (d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes No

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act).

Yes No

The number of shares outstanding of the issuer's class of common stock, as of the latest practicable date:

Common Shares Outstanding at October 26, 2004 is 11,581,780

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PART I FINANCIAL INFORMATION

ITEM 1. Financial Statements

IGI, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF OPERATIONS
(in thousands, except share and per share information)
(Unaudited)

| | Three months ended September 30, | | Nine mo Septe |
|--|-------------------------------------|-----------------------|------------------|
| | 2004 | (as restated) 2003 | 2004 |
| | ----- | ----- | ----- |
| Revenues: | | | |
| Sales, net | \$ 383 | \$ 748 | \$ 2,023 |
| Licensing and royalty income | 199 | 151 | 744 |
| | ----- | ----- | ----- |
| Total revenues | 582 | 899 | 2,767 |
| Cost and expenses: | | | |
| Cost of sales | 244 | 326 | 930 |
| Selling, general and administrative expenses | 320 | 589 | 1,406 |
| Product development and research expenses | 241 | 225 | 1,504 |
| | ----- | ----- | ----- |
| Operating (loss) | (223) | (241) | (1,073) |
| Interest income (expense), net | 6 | - | 21 |
| Loss on sale of investment securities | (1) | - | (1) |
| Other income, net | 1 | - | 1 |
| (Loss) from continuing operations before provision for income taxes | (217) | (241) | (1,052) |
| Provision for income taxes | 2 | 1 | 6 |
| | ----- | ----- | ----- |
| Loss from continuing operations | (219) | (242) | (1,058) |
| | ----- | ----- | ----- |
| Discontinued operations: | | | |
| Gain (loss) on sale of discontinued business | - | (15) | - |
| | ----- | ----- | ----- |
| Net (loss) attributable to common stock | \$ (219) | \$ (257) | \$ (1,058) |
| | ===== | ===== | ===== |
| Basic and Diluted Earnings (Loss) per Common Share | | | |
| Continuing operations | \$ (.02) | \$ (.02) | \$ (.09) |
| Discontinued operations | - | - | - |
| | ----- | ----- | ----- |
| Net (loss) per common share | \$ (.02) | \$ (.02) | \$ (.09) |
| | ===== | ===== | ===== |
| Weighted Average of Common Stock and Common Stock Equivalents Outstanding | | | |
| Basic and diluted | 11,581,780 | 11,355,965 | 11,536,337 |

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The accompanying notes are an integral part of the consolidated financial statements.

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IGI, INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
(in thousands, except share and per share information)

| | September 30, 2004 | December 31, 2003 |
|--|--------------------|-------------------|
| | (unaudited) | |
| ASSETS | | |
| Current assets: | | |
| Cash and cash equivalents | \$ 243 | \$ 82 |
| Restricted cash | 50 | 5 |
| Marketable securities | 574 | 80 |
| Accounts receivable, less allowance for doubtful accounts of \$10 and \$16 in 2004 and 2003, respectively | 208 | 35 |
| Licensing and royalty income receivable | 159 | 1 |
| Inventories | 198 | 19 |
| Prepaid expenses and other current assets | 67 | 13 |
| | 1,499 | 2,36 |
| Total current assets | | 2,36 |
| Property, plant and equipment, net | 2,993 | 2,60 |
| Other assets | 43 | 5 |
| | \$ 4,535 | \$ 5,02 |
| | ===== | ===== |
| LIABILITIES AND STOCKHOLDERS' EQUITY | | |
| Current liabilities: | | |
| Accounts payable | 89 | 10 |
| Accrued payroll | 41 | 7 |
| Other accrued expenses | 313 | 30 |
| Income taxes payable | 9 | |
| Deferred income | 147 | 16 |
| | 599 | 65 |
| Total current liabilities | | 65 |
| Deferred income | 104 | 20 |
| | 703 | 85 |
| | ----- | ----- |
| Commitments and contingencies (Notes 14 and 15) | | |
| Stockholders' equity: | | |
| Common stock \$.01 par value, 50,000,000 shares authorized; 13,547,520 and 13,351,237 shares issued in 2004 and 2003, respectively | 136 | 13 |
| Accumulated other comprehensive income | (35) | |
| Additional paid-in capital | 24,459 | 23,70 |
| Accumulated deficit | (19,333) | (18,27 |
| Less treasury stock at cost, 1,965,740 shares in 2004 and 2003 | (1,395) | (1,39 |

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| | | |
|--|----------|---------|
| Total stockholders' equity | 3,832 | 4,16 |
| Total liabilities and stockholders' equity | \$ 4,535 | \$ 5,02 |

The accompanying notes are an integral part of the consolidated financial statements.

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IGI, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
(in thousands)
(Unaudited)

| | Nine months ended September 30 | |
|--|--------------------------------|---------------|
| | 2004 | 2003 |
| | ---- | ---- |
| | | (as restated) |
| Cash flows from operating activities: | | |
| Net (loss) | \$(1,058) | \$ (570) |
| Reconciliation of net (loss) to net cash used in operating activities: | | |
| Gain on sale of discontinued operations | - | (154) |
| Depreciation and amortization | 206 | 196 |
| Loss on sale of investment securities | 1 | - |
| Provision for accounts and notes receivable and inventories | - | 17 |
| Recognition of deferred income | (119) | (101) |
| Directors' stock issuance | - | 26 |
| Non employee stock options | 537 | - |
| Changes in operating assets and liabilities: | | |
| Accounts receivable | 148 | 27 |
| Inventories | (12) | (23) |
| Receivables due under licensing and royalty agreements | (142) | 67 |
| Prepaid expenses and other assets | 66 | 51 |
| Accounts payable and accrued expenses | (38) | (163) |
| Income taxes payable | 2 | (5) |
| Deferred revenue | - | 42 |
| Net cash used in operating activities | (409) | (590) |
| Cash flows from investing activities: | | |
| Capital expenditures | (581) | (86) |
| Purchase of marketable securities | (110) | (801) |
| Proceeds from sale of marketable securities | 300 | - |
| Increase in other assets | - | 1 |
| Proceeds from sale of discontinued operations | - | 154 |
| Net cash (used in) investing activities | (391) | (732) |
| Cash flows from financing activities: | | |

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| | | |
|---|--------|---------|
| Borrowings from EDA loan | - | 46 |
| Repayment of EDA loan | - | (15) |
| Proceeds from exercise of common stock options and purchase of common stock | 222 | 4 |
| Net increase in marketable securities | - | - |
| Treasury shares purchased | - | (80) |
| | ----- | ----- |
| Net cash provided by (used in) financing activities | 222 | (45) |
| | ----- | ----- |
| Net increase (decrease) in cash and cash equivalents | (578) | (1,367) |
| Cash and cash equivalents at beginning of period | 821 | 1,999 |
| | ----- | ----- |
| Cash and cash equivalents at end of period | \$ 243 | \$ 632 |
| | ===== | ===== |

The accompanying notes are an integral part of the consolidated financial statements.

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IGI, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

1. Basis of Presentation

The accompanying consolidated financial statements have been prepared by IGI, Inc. without audit, pursuant to the rules and regulations of the Securities and Exchange Commission ("SEC"), and reflect all adjustments which, in the opinion of management, are necessary for a fair presentation of the results for the interim periods presented. All such adjustments are of a normal recurring nature.

Certain information in footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted pursuant to the rules and regulations of the SEC, although the Company believes the disclosures are adequate to make the information presented not misleading. These consolidated financial statements should be read in conjunction with the consolidated financial statements and the notes thereto included in the Company's Annual Report on Form 10-K for the year ended December 31, 2003 (the "2003 10-K Annual Report").

Estee Lauder, a significant customer, accounted for \$1,089,000 or 54% of sales for the nine months ended September 30, 2004 and \$1,522,000 or 67% of sales for the nine months ended September 30, 2003. The Company has renegotiated its contract with Estee Lauder. Estee Lauder will be manufacturing all Novasome(R) and non Novasome(R) products in house and will pay the Company a one time payment of \$100,000 plus a royalty per kilo on all Novasome(R) products manufactured by Estee Lauder, including all new products developed. The Company's contract manufacturing of Estee Lauder non-Novasome(R) products, which accounted for \$400,000 of the above sales in 2004, terminated on June 30, 2004, without any future royalties or other payments to be received by the Company on any non-Novasome(R) products manufactured by Estee Lauder. In addition, during the six month period from January through June 2004, the Company agreed to provide Estee Lauder's contract manufacturing services at a reduced price of \$2.00 per kilo, as compared to the prior rate of \$3.03 per kilo. As of September 30,

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2004, a formal agreement with Estee Lauder has not been signed by the Company, but one is anticipated to be signed within the near future.

Prior to filing its Form 10-K for the fiscal year ended December 31, 2003, IGI, Inc, was informed by J&J that there was an error in the calculation of the 2003 royalty due to the company by J&J. The correction of the error resulted in a reduction of revenues, with a corresponding impact on net loss, of \$42,000 in the second qtr of 2003 and \$51,000 in the third quarter of 2003. The restated numbers have been reflected herein.

2. Marketable Securities

Marketable securities at September 30, 2004 consist of an investment in a short term bond mutual fund and an investment in securities. The Company currently classifies all marketable securities as available-for-sale, in accordance with Statement of Financial Accounting Standards (SFAS) 115. Securities classified as available-for-sale are required to be reported at fair value with unrealized gains and losses, net of taxes, excluded from earnings and shown separately as a component of accumulated other comprehensive income within stockholders' equity. Realized gains and losses on the sale of securities available-for-sale are determined using the specific-identification method.

The activity of the available-for-sale marketable securities as of September 30, 2004 is as follows (amounts in thousands):

| | Amortized Cost ----- | Gross Unrealized Gaines ----- | Gross Unrealized Losses ----- | Fair Value ----- | Carrying Amount ----- |
|--------------|----------------------------|--|--|------------------------|-----------------------------|
| Mutual Funds | \$499 | \$ - | \$ (3) | \$496 | \$496 |
| Securities | 110 | - | (32) | 78 | 78 |
| | \$609 | \$ - | \$ (35) | \$574 | \$574 |

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IGI, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited), Continued

Sales of available-for-sale securities for the nine months ended September 30, 2004 were as follows:

| | |
|-----------------------|-------|
| Proceeds from sales | \$300 |
| Gross realized gains | - |
| Gross realized losses | (1) |

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The increase in net unrealized holding losses on available-for-sale securities in the amount of \$35 was charged to stockholders' equity for the nine months ended September 30, 2004.

3. Inventories

Inventories are valued at the lower of cost, using the first-in, first-out ("FIFO") method, or market. Inventories at September 30, 2004 and December 31, 2003 consist of:

| | September 30, 2004 | December 31, 2003 |
|------------------------|--------------------|-------------------|
| (amounts in thousands) | | |
| Finished goods | \$ 19 | \$ 15 |
| Raw materials | 179 | 177 |
| Total | \$198 | \$192 |

4. Stock-Based Compensation

Compensation costs attributable to employee stock option and similar plans are recognized based on the difference, if any, between the quoted market price of the stock on the date of grant over the amount the employee is required to pay to acquire the stock (the intrinsic value method). No stock-based employee compensation cost is reflected in net income for options that have been granted, as all options granted under the plans had an exercise price equal to the market value of the underlying common stock on the date of grant. Since the Company uses the intrinsic value method, it makes pro forma disclosures of net income (loss) and net income (loss) per share as if the fair-value based method of accounting had been applied.

If compensation cost for all grants under the Company's stock option plans had been determined based on the fair value at the grant date consistent with the provisions of Statement of Financial Accounting Standards (SFAS) No. 123, "Accounting for Stock-Based Compensation," the Company's net income (loss) and net income (loss) per share would have changed to the pro forma amounts indicated below:

| | Nine months ended September 30, | |
|--|---|---------|
| | 2004 | 2003 |
| | ---- | ---- |
| | (in thousands, except per share information) | |
| Net income (loss) - as reported | \$(1,058) | \$(570) |
| Deduct: Total stock-based employee compensation expense determined under the fair-value based method (net of tax \$0) | 136 | 20 |
| | ----- | ----- |
| Net income (loss) - pro forma | \$(1,194) | \$(590) |

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| | | |
|---------------------------------------|----------|----------|
| | ===== | ===== |
| Income (loss) per share - as reported | | |
| Basic and diluted | \$ (.09) | \$ (.05) |
| | ===== | ===== |
| Income (loss) per share - pro forma | | |
| Basic and diluted | \$ (.11) | \$ (.05) |
| | ===== | ===== |

The Company recorded a \$537,000 expense related to non employee stock based compensation for the nine months ended September 30, 2004.

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IGI, INC. AND SUBSIDIARIES NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited), Continued

5. Legal and U.S. Regulatory Proceedings

Gallo Matter

As previously reported by the Company in its historical filings with the SEC, including without limitation its Form 10-K for the year ending December 31, 1999, for most of 1997 and 1998 the Company was subject to intensive government regulatory scrutiny by the U.S. Departments of Justice, Treasury and Agriculture. In June 1997, the Company was advised by the Animal and Plant Health Inspection Service ("APHIS") of the United States Department of Agriculture ("USDA") that the Company had shipped quantities of some of its poultry vaccine products without complying with certain regulatory and record keeping requirements. The USDA subsequently issued an order that the Company stop shipment of certain of its products. Shortly thereafter, in July 1997, the Company was advised that the USDA's Office of Inspector General had commenced an investigation into possible violations of the Virus Serum Toxin Act of 1914 and alleged false statements made to APHIS. In April 1998, the SEC advised the Company that it was conducting an informal inquiry and requested information and documents from the Company, which the Company voluntarily provided to the SEC.

Based upon these events, the Board of Directors caused an immediate and thorough investigation of the facts and circumstances of the alleged violations to be undertaken by independent counsel. The Company continued to refine and strengthen its regulatory programs with the adoption of a series of compliance and enforcement policies, the addition of new managers of Production and Quality Control and a new Senior Vice President and General Counsel. At the instruction of the Board of Directors, the Company's General Counsel established and oversaw a comprehensive employee training program, designated in writing a Regulatory Compliance Officer, and established a fraud detection program, as well as an employee "hotline." The Company continued to cooperate with the USDA and SEC in all aspects of their investigation and regulatory activities. On March 13, 2002, the Company reached a settlement with the staff of the SEC to resolve matters arising with respect to the investigation of the Company. Under the settlement, the Company neither admitted nor denied that the Company violated the financial reporting and record-keeping requirements of Section 13 of the Securities and Exchange Act of 1934, as amended, for the three years ended December 31, 1997. Further, the Company agreed to the entry of an order to cease and desist from any

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such violation in the future. No monetary penalty was assessed.

As a result of its internal investigation, in November 1997, the Company terminated the employment of John P. Gallo as President and Chief Operating Officer for willful misconduct. On April 21, 1998, the Company instituted a lawsuit against Mr. Gallo in the New Jersey Superior Court. The lawsuit alleged willful misconduct and malfeasance in office, as well as embezzlement and related claims (referred to as "the IGI Action"). On April 28, 1998, Mr. Gallo instituted a separate action against the Company and two of its Directors, Edward Hager, M.D. and Constantine Hampers, M.D., alleging that he had been wrongfully terminated from employment and further alleging wrongdoings by the two Directors (referred to as the "Gallo Action"). The Court subsequently ordered the consolidation of the IGI Action and the Gallo Action (collectively referred to as the "Consolidated Action").

In response to these allegations, the Company instituted an investigation of the two Directors by an independent committee ("Independent Committee") of the Board assisted by the Company's General Counsel. The investigation included a series of interviews of the Directors, both of whom cooperated with the Company, and a review of certain records and documents. The Company also requested an interview with Mr. Gallo who, through his counsel, declined to cooperate. In September 1998, the Independent Committee reported to the Board that it had found no credible evidence to support Mr. Gallo's claims and allegations and recommended no further action. The Board adopted the recommendation.

The Company denied all allegations plead in the Gallo Action and asserted all claims in the Gallo Action to be without merit. The Company did not reserve any amount relating to such claims. The Company tendered the claim to its insurance carriers, but was denied insurance coverage for both defense and indemnity of the Gallo Action.

In July 1998, the Company sought to depose Mr. Gallo in connection with the Consolidated Action. Through his counsel, Mr. Gallo asserted his Fifth Amendment privilege against self-incrimination and advised that he would not participate in the discovery process until such time as a federal grand jury investigation, in which he was a target, was concluded. In January 1999, at the suggestion of the Court, the Company and Mr. Gallo agreed to a voluntary dismissal without prejudice of the Consolidated Action, with the understanding that the statute of limitations was tolled

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IGI, INC. AND SUBSIDIARIES NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited), Continued

for all parties and all claims, and that the Company and Mr. Gallo were free to reinstate their suits against each other at a later date, with each party reserving all of their rights and remedies against the other.

As of the date hereof, neither the Company nor Mr. Gallo have filed suit against each other in the Superior Court of New Jersey or any other court of competent jurisdiction to reinstitute the claims, in whole or part, previously at issue in the Consolidated Action, and pursuant to the previous order of dismissal entered in the Consolidated Action, the statute of limitation on all claims and

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defenses continues to be tolled as to both parties. However, the Company did receive a letter dated November 21, 2003 from Mr. Gallo's attorneys seeking to reach a settlement of the claims asserted against IGI in the Gallo Action without further resort to the courts. The letter provides a general description of Mr. Gallo's claims and a calculation of damages allegedly sustained by Mr. Gallo relative thereto. The letter states that Mr. Gallo's damages are calculated to be in the range of \$3,400,000 to \$5,100,000. The Company denies liability for the claims and damages alleged in the letter from Mr. Gallo's counsel dated November 21, 2003, and as such, the Company did not make any formal response thereto. Mr. Gallo has contacted the Company's Chief Executive Officer and Chairman, Frank Gerardi, in a continued effort to initiate settlement discussions. As of September 30, 2004, the Company continues to deny any merit and/or liability for the claims alleged by Mr. Gallo and has not engaged in any formal settlement discussions with either Mr. Gallo or his attorneys.

On December 8, 2003, Mr. Gallo filed suit against Novavax, Inc. in the Superior Court of New Jersey, Law Division, Atlantic County, docket no. ATL-L-3388-03, asserting claims under seven counts for damages allegedly sustained as a result of the cancellation of certain Novavax stock options held by Mr. Gallo due to his termination from IGI in November 1997 for willful misconduct (referred to as the "Novavax Action").

On March 5, 2004, Novavax filed an Answer denying the allegations asserted by Mr. Gallo in his First Amended Complaint. In addition, while denying any liability under the First Amended Complaint, Novavax also filed a Third Party Complaint in the Novavax Action against the Company for contribution and indemnification, alleging that if liability for Mr. Gallo's claims is found, the Company has primary liability for any and all such damages sustained.

IGI has been notified by its insurance carriers that coverage is not afforded under their respective policies of insurance for defense and/or indemnification of the claims alleged by the Third Party Complaint. After IGI was notified of the foregoing, but prior to IGI's filing of any responsive pleading, the Third Party Complaint against IGI was voluntarily dismissed without prejudice by Novavax on June 30, 2004. Novavax may at any time pursuant to the rules of court re-file its Third Party Complaint against IGI.

In July 2004, Novavax filed a motion for summary judgment on all claims asserted under Gallo's First Amended Complaint (referred to as "the SJ Motion"). Gallo filed opposition to the SJ Motion contesting all relief sought thereunder. In August 2004, the court held a hearing on the SJ Motion and denied without prejudice the relief sought by the motion for dismissal of Gallo's First Amended Complaint. Upon information and belief, the parties are currently proceeding with discovery in the Novavax Action. The Company as a non-party witness in the Novavax Action was recently served by counsel for Gallo with a subpoena for the production of documents as responsive thereto.

While as of the date hereof, Novavax has not sought to re-file its Third Party Complaint against IGI for which coverage was previously denied by its insurance carriers, but Novavax is not precluded from and may seek to do so in the future.

6. License Agreements

On December 24, 2003, the Company entered into a License Agreement with Dr. Hollick and A&D Bioscience, Inc., a Massachusetts corporation

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wholly owned by Dr. Holick (collectively referred to as "Holick"), whereby Holick granted an exclusive license to the Company to all his rights to the parathyroid hormone related peptide technologies and the glycoside technologies (referred to as "PTH Technologies" and "Glycoside Technologies", respectively) that he developed for various clinical usages including treatment of psoriasis, hair loss and other skin disorders. In consideration for entering into the License Agreement, Holick received up-front a \$50,000 non-refundable payment from the Company. He also received a grant of 300,000 stock options under the Company's authorized stock option plans.

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IGI, INC. AND SUBSIDIARIES NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited), Continued

On April 19, 2004, IGI signed a sublicense agreement with a third party entity, Tarpan Therapeutics, Inc., for the PTH (1-34) technology under which the third party will be obligated at its sole cost and expense to develop and bring the PTH (1-34) technology to market as timely and efficiently as possible, which includes its sole responsibility for the cost of preclinical and clinical development, research and development, manufacturing, laboratory and clinical testing and trials and marketing of products. In addition, the sublicense agreement calls for various payments to IGI throughout the term. IGI was paid a lump sum sublicense fee of \$300,000, from which amount IGI paid the sum of \$232,000, representing the \$236,000 payment due to Dr. Holick in accordance with the terms of his License Agreement with the Company, net of \$4,000 of additional legal fees. Certain subsequent royalty payments received by the Company under the sublicense agreement will be shared with Holick after the Company has recovered any payments previously made to Holick under the License Agreement and an amount equal to the value of the options received by Holick under the License Agreement. The Company is responsible for any and all costs, fees and expenses for the prosecution and oversight of any intellectual property rights related to the licensed technologies. Subject to Holick's early termination right as provided below, the term of the License Agreement is the longer of twenty (20) years or the life of each of the patents thereunder. However, if following 90 days from the effective date of the License Agreement, the Company has not entered into a sublicense agreement for the Glycoside Technologies; Holick has the right to terminate the License Agreement as to the Glycoside Technologies only. Dr. Holick has exercised his right to terminate the License Agreement as to the Glycoside Technologies. The Company is engaged in discussions with the same third party entity for a similar sublicense for the PTH (7-34) technology.

The \$50,000 payment was expensed in the fourth quarter of 2003 and the \$236,000 payment was expensed in the second quarter of 2004 because the PTH and Glycoside Technologies are in a preliminary development phase and do not have any readily determinable alternative future use. The other consideration called for under the License Agreement, such as amounts advanced for the prosecution and oversight of any intellectual property rights related to the licensed technologies which amounted to \$27,500 and the fair value of the 300,000 stock options granted to Holick, which amounted to \$520,000, was also expensed by the Company in the second quarter of 2004 (included in product development and research expenses on the consolidated

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statement of operations), when the sublicense agreement with Tarpan was executed and Holick could no longer terminate the license agreement as it relates to the PTH Technologies and the options became fully vested. The fair value of the stock options was calculated under SFAS 123 using Black Scholes model.

In February 2004, the Company signed a license agreement with Universal Chemical Technologies, Inc. ("UCT") to utilize their patented technology for an electroless nickel boride metal finishing process. This will be a new venture for the Company and will require an initial capital expenditures of approximately \$500,000, of which \$456,000 has been paid to UCT to date to purchase property and equipment and commits the Company to purchase a minimum of \$25,000 of raw materials from UCT in the first year of the license, \$75,000 during the second year and \$150,000 during the third and subsequent years. The Company has also been required to make several building improvements to accommodate the metal finishing equipment. Building improvements have amounted to \$122,000 to date which was paid to various suppliers. The Company is anticipating an additional \$175,000 to be spent to complete the building improvements required, bringing the initial capital expenditures to approximately \$800,000 to complete the metal finishing process line. The Company has hired a new employee to oversee the facility operations at an annual salary of \$60,000 per year. The Company has an exclusive license within a 150 mile radius of its facility for commercial and military applications. Frank Gerardi, the Company's Chairman and Chief Executive Officer, as well as a major IGI shareholder, has personally invested \$350,000 in UCT, which represents less than a 1% ownership interest by Mr. Gerardi in UCT. The Company is anticipating revenues from this venture to begin in the first quarter of 2005.

On July 27, 2004, the Company signed an exclusive license agreement with the University of Massachusetts Medical School (University) for the patented invention entitled "The Treatment of Skin with Adenosine or Adenosine Analogs". The Company intends to encapsulate adenosine or adenosine analogs in its Novasome for use in the skin care field. As consideration of the rights granted in this agreement, the Company has made nonrefundable payments of \$25,000 upon the execution of this agreement and \$25,000 in September 2004. Both of these payments, which amounts to \$50,000, were expensed during the third quarter of 2004 and are included in the product development and research expenses. The agreement also calls for minimum royalty payments of \$25,000 per year commencing on July 27, 2007. If the Company enters into a Sublicense agreement with a third party entity, which it will attempt to do, the Company shall pay the University 50% of all sublicense income.

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IGI, INC. AND SUBSIDIARIES

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

Prior to filing its Form 10-K for the fiscal year ended December 31, 2003, IGI, Inc, was informed by J&J that there was an error in the calculation of the 2003 royalty due to the company by J&J. The correction of the error resulted in a reduction of revenues, with a corresponding impact on net loss, of \$42,000 in the second quarter of 2003 and \$51,000 in the third quarter of 2003. The restated numbers have been reflected herein.

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The following discussion and analysis may contain forward-looking statements. Such statements are subject to certain risks and uncertainties, including those discussed below or in the Company's 2003 10-K Annual Report that could cause actual results to differ materially from the Company's expectations. See "Factors Which May Affect Future Results" below and in the 2003 10-K Annual Report. Readers are cautioned not to place undue reliance on any forward-looking statements, as they reflect management's analysis as of the date hereof. The Company undertakes no obligation to release the results of any revision to these forward-looking statements which may be made to reflect events or circumstances after the date hereof or to reflect the occurrence of anticipated events.

Recent Events

The Company continues discussions with Estee Lauder on revising the way they will do business with them in the future. As of this time, a formal agreement has not been signed by the two entities, but it is anticipated that one will be signed within the next two weeks. Estee Lauder will be manufacturing all Novasome(R) products and pay the Company a royalty per kilo on all Novasome(R) products manufactured by Estee Lauder in-house plus a one time payment of \$100,000. In consideration of the foregoing, Estee Lauder has agreed to release the Company from its contractual exclusivity restrictions, which will now enable the Company to sell its products in department and specialty stores.

On October 27, 2004 the Company announced the signing of a letter of intent for Senetek to acquire IGI in a stock-for-stock transaction in which Senetek shareholders would receive 60% of the shares of a newly formed holding company and IGI shareholders would receive 40%. The holding company would be organized in the United States and would seek listing on either the Nasdaq SmallCap Market or the American Stock Exchange. The transaction is subject to the satisfactory completion by each company of a due diligence review of the other company's business, technology, financial position and prospects, negotiation and execution of definitive agreements and their approval by the companies' respective Boards of Directors and shareholders, and satisfaction of all closing conditions specified in the definitive agreements. In addition, if the combined market capitalizations of the two companies, based on the average daily sale prices of their shares during a 20-trading day period following circulation of their respective proxy statements for the transaction, is less than \$40 million (equivalent to a minimum of \$16 million pro forma value for the 40% of the combined company's shares issuable to IGI shareholders), either party may terminate the transaction. IGI has agreed not to enter into any discussions with third parties for a possible business combination or other transaction not in the ordinary course of business for a period of 60 days while the due diligence investigations continue, although it may provide publicly available information pursuant to confidentiality agreements signed with third parties prior to the date of the letter of intent.

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IGI, INC. AND SUBSIDIARIES

ITEM 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (Continued)

Results of Operations

Three months ended September 30, 2004 compared to September 30, 2003

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The Company had net loss of \$219,000, or (\$.02) per share, for the quarter ended September 30, 2004 compared to net loss of \$257,000, or (\$.02) per share, for the quarter ended September 30, 2003.

Total revenues for the quarter ended September 30, 2004 were \$582,000, compared to \$899,000 for the quarter ended September 30, 2003, or a \$317,000 decrease. The decrease is primarily due to the loss of product sales to Estee Lauder during the quarter ended September 30, 2004.

As a percentage of product sales, cost of sales was 64% for the quarter ended September 30, 2004 and 44% for the quarter ended September 30, 2003. The increase in cost of sales was also a result of the loss of product sales to Estee Lauder for the quarter ended September 30, 2004, Estee Lauder product were sold at a higher gross margin percentage than other products resulting in the higher cost of sales for this quarter.

Selling, general and administrative expenses decreased \$269,000, or 46%, from \$589,000 in the quarter ended September 30, 2003. As a percentage of revenues, these expenses were 55% of revenues in the third quarter of 2004 compared to 66% for the second quarter of 2004. Overall, expenses decreased primarily due to lower executive salaries, travel and entertainment costs.

Product development and research expenses increased \$16,000, or 7%, compared to the quarter ended September 30, 2003. The increase in expenses is mainly a result of the \$50,000 payment to the University of Massachusetts in the quarter ended September 30, 2004 and new projects that are being worked on for existing and potential new customers.

Interest income increased from \$0 in the quarter ended September 30, 2003 to \$6,000 in the quarter ended September 30, 2004 from investments made in the current year.

Nine months ended September 30, 2004 compared to September 30, 2003

The Company had a net loss attributable to common stock of \$1,058,000, or (\$.09) per share, for the nine months ended September 30, 2004 compared to net loss attributable to common stock of \$570,000, or (\$.05) per share, for the nine months ended September 30, 2003.

Total revenues for the nine months ended September 30, 2004 were \$2,767,000, which represents a increase of \$16,000, or 1%, from revenues of \$2,751,000 for the nine months ended September 30, 2003. The increase in revenues was due to a higher royalty revenues in the nine months ended September 30, 2004 from Estee Lauder and Tarpan Therapeutics offset by a loss of product sales from Estee Lauder and lower royalties from Johnson and Johnson. On June 30, 2004, the Company's revenue from Estee Lauder switched from product revenue to royalty revenue.

Cost of sales, as a percent of product sales, increased from 45% for the nine months ended September 30, 2003 to 46% for the nine months ended September 30, 2004. The increase in cost of sales was also a result of the loss of product sales to Estee Lauder for the quarter ended September 30, 2004, Estee Lauder product were sold at a higher gross margin percentage than other products resulting in the higher cost of sales for this quarter.

Selling, general and administrative expenses decreased \$535,000, or 28%, from \$1,941,000 for the nine months ended September 30, 2003. As a percent of revenues, these expenses were 71% of revenues for the first nine months of 2003 compared to 51% for the first nine months of 2004. The decrease is primarily due to a decline in salary and travel expenses from the elimination of three positions within the company during 2004.

IGI, INC. AND SUBSIDIARIES

ITEM 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (Continued)

Product development and research expenses increased \$976,000, or 185%, compared to the nine months ended September 30, 2003. The increase in expenses is a mainly a result of a non cash expense of \$548,000 being recorded in the second quarter of 2004 related to the SFAS 123 value of 300,000 stock options granted to Dr. Holick under his license agreement and 25,000 stock options granted to Dr. Holick for his service on the Scientific Advisory Board, plus a cash payment made to Dr. Holick in accordance with his license agreement in the amount of \$232,000.

Also, there was a \$50,000 payment made to University of Massachusetts in accordance with their agreement. In addition, new projects are being worked on for existing and potential new customers and there are additional personnel.

Interest income increased \$13,000 compared to the nine months ended September 30, 2003. The increase is due to higher interest rates on cash investments and better return on funds invested in mutual funds.

Liquidity and Capital Resources

The Company's operating activities used \$409,000 of cash during the nine months ended September 30, 2004 compared to \$590,000 used in the comparable period of 2003. Payments for professional fees and payments made to Dr. Holick in accordance with his license agreement, offset by lower salaries were the primary uses of cash in 2004.

The Company used \$391,000 of cash in the nine months ended September 30, 2004 for investing activities compared to \$732,000 used in investing activities in the first nine months of 2003. Payments to Universal Chemical Technologies, Inc. ("UCT") and other various vendors amounting to \$581,000 was used to purchase machinery and equipment related to the electroless nickel boride finishing operations that will be set up in the Company's Buena facility, which was offset by sales of marketable securities amounting to \$300,000, while 2003's investing activities were for the purchase of marketable securities.

The Company's financing activities provided \$222,000 of cash in the nine months ended September 30, 2004 compared to \$45,000 utilized by financing activities in the nine months ended September 30, 2003. The cash provided in 2004 represents proceeds from the exercise of stock options. The cash utilized in 2003 is primarily the result of the purchase of Company stock as part of a stock buy-back program, offset by funding from the EDA loan.

The Company's principal sources of liquidity are cash from operations, cash and cash equivalents and marketable securities. The Company has undergone many changes within the passed six months, the release of the exclusivity on the Estee Lauder contract which coincided with the loss of the Company manufacturing products for Estee Lauder, along with our expansion of the facility to house the metal plating line for UCT. These changes have made it necessary for the Company to utilize its cash. However, these changes were necessary to enable the Company for growth and expansion. Management was aware of the impact that these changes would have on the cash balance and management believes that existing cash and cash equivalents, marketable

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securities and cash flows from operations will be sufficient to meet the Company's foreseeable cash needs for at least the next year. If these funds are not sufficient, two shareholders of the Company have agreed to loan the Company up to \$500,000 each, if necessary, to fund the Company's deficit through June 30, 2005 and other members of the board have agreed to exercise stock options to raise capital, if needed. There may be acquisition and other growth opportunities; however that require additional external financing. Management may, from time to time, seek to obtain additional funds from the public or private issuances of equity or debt securities. There can be no assurance that such financings will be available or available on terms acceptable to the Company.

There have been no material changes to the Company's contractual commitments as reflected in the 2003 10-K Annual Report other than those disclosed in this Form 10-Q.

Factors Which May Affect Future Results

The industry segments in which the Company competes are subject to intense competitive pressures. The following sets forth some of the risks which the Company faces.

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IGI, INC. AND SUBSIDIARIES

ITEM 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (Continued)

Intense Competition in Consumer Products Business

The Company's Consumer Products business competes with large, well-financed cosmetics and consumer products companies with development and marketing groups that are experienced in the industry and possess far greater

resources than those available to the Company. There is no assurance that the Company's consumer products can compete successfully against its competitors or that it can develop and market new products that will be favorably received in the marketplace. In addition, certain of the Company's customers that use the Company's Novasome(R) lipid vesicles in their products may decide to reduce their purchases from the Company or shift their business to other suppliers.

Effect of Rapidly Changing Technologies

The Company expects to sublicense its technologies to third parties, which would manufacture and market products incorporating the technologies. However, if its competitors develop new and improved technologies that are superior to the Company's technologies, its technologies could be less acceptable in the marketplace and therefore the Company's planned technology sublicensing could be materially adversely affected.

Revision of Current Contract with Estee Lauder

Previously, the Company manufactured Novasome(R) products and contract manufacturing products for Estee Lauder using the raw materials supplied by Estee Lauder. The Company is currently renegotiating its agreement with

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Estee Lauder. The Company anticipates that the revised agreement will end all contract manufacturing. The Company also anticipates that Estee Lauder will manufacture Novasome(R) products in house and will pay the Company a one time payment of \$100,000 plus a royalty on the volume produced. In addition, Estee Lauder will remove the exclusivity clause which will allow the Company to sell its products in department and specialty stores. Although it is the Company's belief that this will increase business and revenue in the future, there is no guarantee that it will occur.

Licensing Agreement with Universal Chemical Technologies, Inc.

In February 2004, the Company signed a license agreement with UCT to utilize their patented technology for an electroless nickel boride metal finishing process. This will be a new venture for the Company and will require significant capital expenditures in the Company's existing manufacturing facility to set up the operations. The Company is also obligated to purchase a minimum level of raw materials from UCT during the license term. The Company has an exclusive license within a 150 mile radius of its facility for commercial and military applications. Frank Gerardi, the Company's Chairman and Chief Executive Officer, as well as a major IGI shareholder, has personally invested \$350,000 in UCT, which represents less than a 1% ownership interest by Mr. Gerardi in UCT. The Company believes there is the possibility of major revenue and profit growth using this application, but there is no guarantee that it will materialize.

American Stock Exchange (AMEX) Continuing Listing Standards

On March 28, 2002, the Company was notified by AMEX that it was below certain of the Exchange's continuing listing standards. Specifically, the Company was required to reflect income from continuing operations and net income for 2002 and a minimum of \$4,000,000 in stockholders' equity by December 31, 2002 in order to remain listed.

On April 25, 2002, the Company submitted a plan of compliance to AMEX. On June 12, 2002, AMEX notified the Company that it had accepted the Company's plan of compliance and had granted the Company an extension of time to regain compliance with the continued listing standards by December 31, 2002. The Company was subject to periodic review by the AMEX staff during the extension period. Based on the Company's reported results for 2002, the Company was not in compliance with the AMEX listing standards for income from continuing operations. On April 14, 2003, the Company received formal notification from AMEX that the Company was deemed to be in compliance with all AMEX requirements for continued listing on AMEX. This determination is subject to the Company's favorable

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IGI, INC. AND SUBSIDIARIES

ITEM 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (Continued)

progress in satisfying the AMEX guidelines for continued listing and to AMEX's routine periodic reviews of the Company's SEC filings. Based on the Company's 2003 year-end results, the Company was not in compliance with the AMEX requirement for reporting income from continuing operations and net income for the year ended December 31, 2003.

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As of the date of the filing of the Form 10-Q for the quarter ended September 30, 2004, the Company has not been contacted by AMEX concerning the Company's non-compliance with the AMEX requirements. While as of this date, the Company has not received any notification of non-compliance from AMEX, the Company has no knowledge of nor can it predict whether AMEX shall at any time hereafter issue formal notification to the Company of its non-compliance with the requirements for continued listing on AMEX, which could result in the Company's delisting from AMEX or otherwise adversely affect the Company.

Critical Accounting Policies

There have been no material changes to the Company's critical accounting policies as reflected in the 2003 10-K Annual Report.

ITEM 3. Quantitative and Qualitative Disclosures about Market Risk

Market risk represents the risk of loss that may impact the financial position, results of operations, or cash flow of the Company due to adverse changes in market prices and interest rates. The Company is exposed to market risk because of changes in interest rates and changes in the fair market value of its marketable securities portfolio.

The Company does not use derivatives for any hedging or speculative strategies. Accordingly, at September 30, 2004, the Company is not a party to any derivative transactions. The Company classifies its investments in its marketable securities portfolio as available-for-sale and records them at fair value. The securities unrealized holding gains and losses are excluded from income and are recorded directly to stockholders' equity in accumulated other comprehensive income. Changes in interest rates are not expected to have an adverse effect on the Company's financial condition or results of operations.

ITEM 4. Controls and Procedures

Under the supervision and with the participation of certain members of the Company's management, including the Chief Executive Officer and Vice President of Finance, the Company completed an evaluation of the effectiveness of the design and operation of its disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) to the Securities Exchange Act of 1934, as amended (the "Exchange Act")). Based on this evaluation, the Company's Chief Executive Officer and Vice President of Finance believe that the disclosure controls and procedures were effective as of the end of the period covered by this report with respect to timely communicating to them and other members of management responsible for preparing periodic reports all material information required to be disclosed in this report as it relates to the Company and its consolidated subsidiaries.

The Company's management does not expect that its disclosure controls and procedures or its internal control over financial reporting will prevent all errors and all fraud. A control system, no matter how well conceived and operated, can provide only reasonable, as opposed to absolute, assurance that the objectives of the control system are met. Further, the design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within the Company have been detected.

These inherent limitations include the realities that judgments in decision-

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making can be faulty, and breakdowns can occur because of simple errors or mistakes. Additionally, controls can be circumvented by the individual acts of some person or by collusion of two or more people. The design of any system of controls also is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions; over time, controls may become inadequate because

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ITEM 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (Continued)

of changes in conditions, or the degree of compliance with the policies or procedures may deteriorate. Because of the inherent limitations in a cost-effective control system, misstatements due to error or fraud may occur and not be detected. Accordingly, the Company's disclosure controls and procedures are designed to provide reasonable, not absolute, assurance that the objectives of its disclosure control system are met and, as set forth above, the Company's management has concluded, based on their evaluation as of the end of the period, that the Company's disclosure controls and procedures were sufficiently effective to provide reasonable assurance that the objectives of the disclosure control system were met.

There was no change in the Company's internal control over financial reporting during the Company's last fiscal quarter that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

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IGI, INC. AND SUBSIDIARIES PART II OTHER INFORMATION

ITEM 1. Legal Proceedings

Gallo Matter

As previously reported by the Company in its historical filings with the Securities and Exchange Commission ("SEC"), including without limitation its Form 10-K for the year ending December 31, 1999, for most of 1997 and 1998 the Company was subject to intensive government regulatory scrutiny by the U.S. Departments of Justice, Treasury and Agriculture. In June 1997, the Company was advised by the Animal and Plant Health Inspection Service ("APHIS") of the United States Department of Agriculture ("USDA") that the Company had shipped quantities of some of its poultry vaccine products without complying with certain regulatory and record keeping requirements. The USDA subsequently issued an order that the Company stop shipment of certain of its products. Shortly thereafter, in July 1997, the Company was advised that the USDA's Office of Inspector General had commenced an investigation into possible violations of the Virus Serum Toxin Act of 1914 and alleged false statements made to APHIS. In April 1998, the SEC advised the Company that it was conducting an informal inquiry and requested information and documents from the Company, which the Company voluntarily provided to the SEC.

Based upon these events, the Board of Directors caused an immediate and

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thorough investigation of the facts and circumstances of the alleged violations to be undertaken by independent counsel. The Company continued to refine and strengthen its regulatory programs with the adoption of a series of compliance and enforcement policies, the addition of new managers of Production and Quality Control and a new Senior Vice President and General Counsel. At the instruction of the Board of Directors, the Company's General Counsel established and oversaw a comprehensive employee training program, designated in writing a Regulatory Compliance Officer, and established a fraud detection program, as well as an employee "hotline." The Company continued to cooperate with the USDA and SEC in all aspects of their investigation and regulatory activities. On March 13, 2002, the Company reached a settlement with the staff of the SEC to resolve matters arising with respect to the investigation of the Company. Under the settlement, the Company neither admitted nor denied that the Company violated the financial reporting and record-keeping requirements of Section 13 of the Securities and Exchange Act of 1934, as amended, for the three years ended December 31, 1997. Further, the Company agreed to the entry of an order to cease and desist from any such violation in the future. No monetary penalty was assessed.

As a result of its internal investigation, in November 1997, the Company terminated the employment of John P. Gallo as President and Chief Operating Officer for willful misconduct. On April 21, 1998, the Company instituted a lawsuit against Mr. Gallo in the New Jersey Superior Court. The lawsuit alleged willful misconduct and malfeasance in office, as well as embezzlement and related claims (referred to as "the IGI Action"). On April 28, 1998, Mr. Gallo instituted a separate action against the Company and two of its Directors, Edward Hager, M.D. and Constantine Hampers, M.D., alleging that he had been wrongfully terminated from employment and further alleging wrongdoings by the two Directors (referred to as the "Gallo Action"). The Court subsequently ordered the consolidation of the IGI Action and the Gallo Action (collectively referred to as the "Consolidated Action").

In response to these allegations, the Company instituted an investigation of the two Directors by an independent committee ("Independent Committee") of the Board assisted by the Company's General Counsel. The investigation included a series of interviews of the Directors, both of whom cooperated with the Company, and a review of certain records and documents. The Company also requested an interview with Mr. Gallo who, through his counsel, declined to cooperate. In September 1998, the Independent Committee reported to the Board that it had found no credible evidence to support Mr. Gallo's claims and allegations and recommended no further action. The Board adopted the recommendation.

The Company denied all allegations plead in the Gallo Action and asserted all claims in the Gallo Action to be without merit. The Company did not reserve any amount relating to such claims. The Company tendered the claim to its insurance carriers, but was denied insurance coverage for both defense and indemnity of the Gallo Action.

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IGI, INC. AND SUBSIDIARIES PART II OTHER INFORMATION, Continued

In July 1998, the Company sought to depose Mr. Gallo in connection with the Consolidated Action. Through his counsel, Mr. Gallo asserted his Fifth Amendment privilege against self-incrimination and advised that he would not participate in the discovery process until such time as a federal grand jury

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investigation, in which he was a target, was concluded. In January 1999, at the suggestion of the Court, the Company and Mr. Gallo agreed to a voluntary dismissal without prejudice of the Consolidated Action, with the understanding that the statute of limitations was tolled for all parties and all claims, and that the Company and Mr. Gallo were free to reinstate their suits against each other at a later date, with each party reserving all of their rights and remedies against the other.

As of the date hereof, neither the Company nor Mr. Gallo have filed suit against each other in the Superior Court of New Jersey or any other court of competent jurisdiction to reinstitute the claims, in whole or part, previously at issue in the Consolidated Action, and pursuant to the previous order of dismissal entered in the Consolidated Action, the statute of limitation on all claims and defenses continues to be tolled as to both parties. However, the Company did receive a letter dated November 21, 2003 from Mr. Gallo's attorneys seeking to reach a settlement of the claims asserted against IGI in the Gallo Action without further resort to the courts. The letter provides a general description of Mr. Gallo's claims and a calculation of damages allegedly sustained by Mr. Gallo relative thereto. The letter states that Mr. Gallo's damages are calculated to be in the range of \$3,400,000 to \$5,100,000. The Company denies liability for the claims and damages alleged in the letter from Mr. Gallo's counsel dated November 21, 2003, and as such, the Company did not make any formal response thereto. Mr. Gallo has contacted the Company's Chief Executive Officer and Chairman, Frank Gerardi, in a continued effort to initiate settlement discussions. As of the present date, the Company continues to deny any merit and/or liability for the claims alleged by Mr. Gallo and has not engaged in any formal settlement discussions with either Mr. Gallo or his attorneys.

On December 8, 2003, Mr. Gallo filed suit against Novavax, Inc. in the Superior Court of New Jersey, Law Division, Atlantic County, docket no. ATL-L-3388-03, asserting claims under seven counts for damages allegedly sustained as a result of the cancellation of certain Novavax stock options held by Mr. Gallo due to his termination from IGI in November 1997 for willful misconduct (referred to as the "Novavax Action").

On March 5, 2004, Novavax filed an Answer denying the allegations asserted by Mr. Gallo in his First Amended Complaint. In addition, while denying any liability under the First Amended Complaint, Novavax also filed a Third Party Complaint in the Novavax Action against the Company for contribution and indemnification, alleging that if liability for Mr. Gallo's claims is found, the Company has primary liability for any and all such damages sustained.

IGI has been notified by its insurance carriers that coverage is not afforded under their respective policies of insurance for defense and/or indemnification of the claims alleged by the Third Party Complaint. After IGI was notified of the foregoing, but prior to IGI's filing of any responsive pleading, the Third Party Complaint against IGI was voluntarily dismissed without prejudice by Novavax on June 30, 2004. Novavax may at any time pursuant to the rules of court re-file its Third Party Complaint against IGI.

In July 2004, Novavax filed a motion for summary judgment on all claims asserted under Gallo's First Amended Complaint (referred to as "the SJ Motion"). Gallo filed opposition to the SJ Motion contesting all relief sought thereunder. In August 2004, the court held a hearing on the SJ Motion and denied without prejudice the relief sought by the motion for dismissal of Gallo's First Amended Complaint. Upon information and belief, the parties are currently proceeding with discovery in the Novavax Action. The Company as a non-party witness in the Novavax Action was recently served by counsel for Gallo with a subpoena for the production of documents as responsive

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thereto.

While as of the date hereof, Novavax has not sought to re-file its Third Party Complaint against IGI for which coverage was previously denied by its insurance carriers, but Novavax is not precluded from and may seek to do so in the future.

ITEM 2. Unregistered Sales of Equity Securities and Use of Proceeds

None.

ITEM 3. Defaults Upon Senior Securities

None.

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IGI, INC. AND SUBSIDIARIES PART II OTHER INFORMATION, Continued

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

None.

ITEM 5. Other Information

None.

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IGI, INC. AND SUBSIDIARIES PART II OTHER INFORMATION, Continued

ITEM 6. Exhibits and Reports on Form 8-K

(a) Exhibits

31.1 Certification of the Chairman and Chief Executive Officer Pursuant to Rule 13a-14(a) under the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

31.2 Certification of the Vice President of Finance Pursuant to Rule 13a-14(a) under the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

32.1 Certification of the Chairman and Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as enacted under Section 906 of the Sarbanes-Oxley Act of 2002.

32.2 Certification of the Vice President of Finance pursuant to 18 U.S.C. Section 1350, as enacted under Section 906 of the Sarbanes-Oxley Act of 2002.

(b) Reports on Form 8-K. The following reports on Form 8-K have been filed

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during the quarter for which this report is filed:

Form 8-K filed October 28, 2004, on which Item 8.01 was completed to announce IGI signing of a letter of intent for Senetek PLC to acquire IGI in a stock-for-stock transaction.

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IGI, INC. AND SUBSIDIARIES

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.

IGI, Inc.
(Registrant)

Date: November 11, 2004

By: /s/ Frank Gerardi

Frank Gerardi
Chairman and Chief Executive Officer

Date: November 11, 2004

By: /s/ Carlene Lloyd

Carlene Lloyd
Vice President, Finance

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