INTEGRATED BIOPHARMA INC
Form 10-Q
February 20, 2009

UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington D.C. 20549

FORM 10-Q

| X | Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the quarterly period ended December 31, 2008

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 001-31668

INTEGRATED BIOPHARMA, INC.

(Exact name of registrant, as specified in its charter)

Delaware	**22-2407475**
(State or other jurisdiction of incorporation or organization)	*(I.R.S. Employer Identification No.)*

225 Long Ave., Hillside, New Jersey	**07205**
(Address of principal executive offices)	*(Zip Code)*

(888) 319-6962

(Registrant's telephone number, including Area Code)

Not Applicable

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

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities and 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 þ No o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer o Accelerated filer o Non-accelerated filer o Smaller reporting company þ

Indicate by check whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes o No þ

Applicable only to Corporate Issuers:

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

Class	*Outstanding at February 13, 2009*
Common Stock, $0.002 par value	20,207,343 Shares

INTEGRATED BIOPHARMA, INC. AND SUBSIDIARIES

FORM 10-Q QUARTERLY REPORT

For the Six Months Ended December 31, 2008

INDEX

		Page
	Part I. Financial Information	
Item 1.	Condensed Consolidated Statements of Operations for the Three and Six Months Ended December 31, 2008 and 2007 (unaudited)	2
	Condensed Consolidated Balance Sheets as of December 31, 2008 (unaudited) and June 30, 2008	3
	Condensed Consolidated Statements of Changes in Stockholders' Equity for the Six Months Ended December 31, 2008 (unaudited)	4
	Condensed Consolidated Statements of Cash Flows for the Six Months Ended December 31, 2008 and 2007 (unaudited)	5
	Notes to Condensed Consolidated Statements	6
Item 2.	Management's Discussion and Analysis of Financial Condition and Results of Operations	21
Item 3.	Quantitative and Qualitative Disclosures about Market Risk	29
Item 4T.	Controls and Procedures	29
	Part II. Other Information	
Item 1.	Legal Proceedings	31
Item 1A.	Risk Factors	31
Item 2.	Unregistered Sales of Equity Securities and Use of Proceeds	31
Item 3.	Defaults Upon Senior Securities	31
Item 4.	Submission of Matters to a Vote of Security Holders	31
Item 5.	Other Information	32
Item 6.	Exhibits	32
	Other	
Signatures		34

Disclosure Regarding Forward-Looking Statements

Certain statements in the Quarterly Report on Form 10-Q may constitute “forward-looking” statements as defined in Section 27A of the Securities Act of 1933, as amended (the “Securities Act”), Section 21E of the Securities Act of 1934, as amended (the “Exchange Act”), the Private Securities Litigation Reform Act of 1995 (the “PSLRA”) or in releases made by the Securities and Exchange Commission, all as may be amended from time to time. Such forward-looking statements involve known and unknown risks, uncertainties and other factors which may cause the actual results, performance or achievements of Integrated BioPharma, Inc. (the “Company”) or industry results, to be materially different from any future results, performance or achievements expressed or implied by such forward-looking statements. Statements that are not historical fact are forward-looking statements. Forward-looking statements can be identified by, among other things, the use of forward-looking language, such as the words, “plan”, “believe”, “expect”, “anticipate”, “intend”, “estimate”, “project”, “may”, “will”, “would”, “could”, “should”, “seeks”, or “scheduled to”, or other s the negative of these terms or other variations of these terms or comparable language, or by discussion of strategy or intentions. These cautionary statements are being made pursuant to the Securities Act, the Exchange Act and the PSLRA with the intention of obtaining the benefits of the “safe harbor” provisions of such laws. The Company cautions investors that any forward-looking statements made by the Company are not guarantees or indicative of future performance. Important assumptions and other important factors that could cause actual results to differ materially from those forward-looking statements with respect to the Company, include, but are not limited to, the risks and uncertainties affecting its businesses described in Items 1 and 1A of the Company’s Annual Report filed on Form 10-K for the year ended June 30, 2008 and in registration statements and other securities filings by the Company.

Although the Company believes that its plans, intentions and expectations reflected in or suggested by such forward-looking statements are reasonable, actual results could differ materially from a projection or assumption in any of its forward-looking statements, are subject to change and inherent risks and uncertainties. The forward-looking statements contained in this Quarterly Report on Form 10-Q are made only as of the date hereof and the Company does not have or undertake any obligation to update or revise any forward-looking statements whether as a result of new information, subsequent events or otherwise, unless otherwise required by law.

ITEM 1. FINANCIAL STATEMENTS

2

5

INTEGRATED BIOPHARMA, INC. AND SUBSIDIARIES
NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
AS OF DECEMBER 31, 2008 AND JUNE 30, 2008 AND FOR THE
THREE AND SIX MONTHS ENDED DECEMBER 31, 2008 AND 2007

(in thousands, except share and per share amounts)

Note 1. Principles of Consolidation, Liquidity and Basis of Presentation

The accompanying financial statements for the interim periods are unaudited and include the accounts of the Company. The interim financial statements have been prepared in conformity with Rule 10-01 of Regulation S-X of the Securities and Exchange Commission ("SEC") and therefore do not include information or footnotes necessary for a complete presentation of financial position, results of operations and cash flows in conformity with accounting principles generally accepted in the United States of America. However, all adjustments (consisting only of normal recurring adjustments) which are, in the opinion of management, necessary for a fair presentation of the financial position and operating results for the periods presented have been included. These financial statements should be read in conjunction with the financial statements and notes thereto, together with Management's Discussion and Analysis of Financial Condition and Results of Operations, contained in the Company's Annual Report on Form 10-K for the fiscal year ended June 30, 2008 ("10-K"), as filed with the SEC. The June 30, 2008 balance sheet was derived from audited financial statements, but does not include all disclosures required by accounting principles generally accepted in the United States of America. The results of operations for the three and six months ended December 31, 2008 are not necessarily indicative of the results for the full fiscal year ending June 30, 2009 or for any other period.

Integrated BioPharma, Inc., a Delaware corporation (together with its subsidiaries, the "Company" or "INB"), is engaged primarily in manufacturing, distributing, marketing and sales of vitamins, nutritional supplements and herbal products; the manufacture and distribution of Paclitaxel, which is the primary chemotherapeutic agent in the treatment of breast cancer and pharmaceutical technical services through its contract research organization. The Company's customers are located primarily in the United States. The Company was previously known as Integrated Health Technologies, Inc. and, prior to that, as Chem International, Inc. The Company was reincorporated in its current form in Delaware in 1995. The Company is registered on the NASDAQ Global Market and its common stock trades using the symbol "INBP". The Company continues to do business as Chem International, Inc. with its customers and certain vendors.

The Nutraceutical segment includes: InB:Manhattan Drug Company, Inc. ("Manhattan Drug"), which manufactures vitamins and nutritional supplements for sale to distributors, multilevel marketers and specialized health-care providers; AgroLabs, Inc., which manufactures products carrying the "Naturally" label and natural and organic product ingredients; The Vitamin Factory and Scientific Sports Nutrition, which sells private label Manhattan Drug products through mail order catalogs and the Internet and through wholesalers and distributors targeting consumers who are professional, amateur and recreational athletes, respectively. The Company also distributes fine natural chemicals through its wholly-owned subsidiary IHT Health Products, Inc. During fiscal year 2007, The Organic Beverage Company (TOBC), formerly Bioscience Technologies, Inc., completed the acquisition from BevSpec, Inc. ("BevSpec") of the Syzmo™ product, which is a USDA organic energy drink. During the first quarter of the fiscal year ending 2009, the Company curtailed operations of its TOBC subsidiary and combined the sales efforts for this product line with the AgroLabs products.

The Pharmaceutical segment includes InB:Paxis Pharmaceuticals, Inc. ("Paxis") and InB:Hauser Pharmaceutical

Services, Inc. (“Hauser”). Paxis manufactures and distributes Paclitaxel, which is the primary chemotherapeutic agent in the treatment of breast cancer. Hauser is a contract research organization (“CRO”) which provides research, development manufacturing at testing services to the specialty chemical, pharmaceutical and natural products industries. In September 2008, the Company announced the engagement of an investment advisor to explore selling substantially all of the Pharmaceutical segment’s net assets.

The Biotechnologies segment included iBioPharma, Inc. (“iBio”), which was focused on the discovery, development and commercialization of proprietary products from plants. On August 18, 2008, the Company’s distribution of the Biotechnologies segment was completed and each shareholder of Integrated BioPharma, Inc.

received one share of iBio's common stock for each share the shareholder owned as of August 12, 2008, the Record Date (See Note 2. Discontinued Operations).

Liquidity. As of December 31, 2008, the Company has working capital deficit of $342 caused primarily by the Notes Payable outstanding in the amount of $7,016 with a principal amount of $7,805 due November 15, 2009 being classified as a current liability. The Company's expected return to profitability in the latter months of fiscal year 2009, which cannot be assured (although it still expects to report a loss for fiscal year 2009), could provide a portion of cash needs over the ensuing twelve-month period to meet capital expenditure needs and daily operational needs. In addition, in February 2009 the Company obtained a Working Capital Bridge Loan from a related party, major shareholder and director, (see Note 13. Subsequent Events) and the Company may sell or otherwise dispose of substantially all of the net assets of the Pharmaceutical segment to further fund its cash needs. Even with the expected return to profitability, the Working Capital Bridge Loan and the potential to sell or otherwise dispose of Company assets, the Company's current cash flows will not be able to repay the Notes Payable without refinancing, or obtaining additional debt or capital from other sources. There can be no assurance that the Company will be successful in these efforts, which raises substantial doubt as to the Company's ability to continue as a going concern. The consolidated financial statements do not include any adjustments that might result from the outcome of this uncertainty.

Reclassifications. Certain reclassifications have been made to the prior year data to conform with the current year presentation.

Principles of Consolidation. The accompanying condensed consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries, and any majority-owned investment. Intercompany transactions and accounts are eliminated in consolidation.

Estimates. The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Management bases its estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. The most significant estimates include:

- sales returns and allowances;
- trade marketing and merchandising;
- allowance for doubtful accounts;
- inventory valuation;
-

valuation and recoverability of long-lived and intangible assets, including the values assigned to acquired intangible assets;

- income taxes and valuation allowance on deferred income taxes, and;

- accruals for, and the probability of, the outcome of current litigation.

On a continual basis, management reviews its estimates utilizing currently available information, changes in facts and circumstances, historical experience and reasonable assumptions. After such reviews, and if deemed appropriate, those estimates are adjusted accordingly. Actual results could differ from those estimates. Nothing has come to our attention which would cause a change in these estimates.

Revenue Recognition. For product sales, the Company recognizes revenue when the product's title and risk of loss transfers to the customer. The Company believes this revenue recognizing practice is appropriate because the Company's sales policies meet the four criteria of SAB 104 which are: (i) persuasive evidence that an arrangement exists, (ii) delivery has occurred, (iii) the seller's price to the buyer is fixed and determinable and (iv) collectability is reasonably assured. The Company's sales policy is to require customers to provide purchase

INTEGRATED BIOPHARMA, INC. AND SUBSIDIARIES
NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
AS OF DECEMBER 31, 2008 AND JUNE 30, 2008 AND FOR THE
THREE AND SIX MONTHS ENDED DECEMBER 31, 2008 AND 2007

(in thousands, except share and per share amounts)

orders establishing selling prices and shipping terms. The Company evaluates the credit risk of each customer and establishes an allowance of doubtful accounts for any credit risk. Sales returns and allowances are estimated upon shipment. The Company recognizes income in its Hauser subsidiary upon monthly customer invoicing. The invoice amount is based upon time and materials spent in the month.

Shipping and Handling Costs. Shipping and handling costs are included in cost of sales.

Trade Marketing and Merchandising. In order to support the Company's proprietary Nutraceutical product lines, various promotional activities are conducted through the retail trade, distributors or directly with consumers, including in-store display and product placement programs, feature price discounts, coupons, and other similar activities. The Company regularly reviews and revises, when it deems necessary, estimates of costs to the Company for these promotional programs based on estimates of what will be redeemed by the retail trade, distributors, or consumers. These estimates are made using various techniques, including historical data on performance of similar promotional programs. Differences between estimated expense and actual performance are generally not material and are recognized as a change in management's estimate in a subsequent period.

Supplemental Statement of Cash Flows

INTEGRATED BIOPHARMA, INC. AND SUBSIDIARIES
NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
AS OF DECEMBER 31, 2008 AND JUNE 30, 2008 AND FOR THE
THREE AND SIX MONTHS ENDED DECEMBER 31, 2008 AND 2007
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Earnings Per Share. In accordance with FASB Statement No. 128, "Earnings Per Share," basic earnings per common share are based on weighted average number of common shares outstanding. Diluted earnings per share amounts are based on the weighted average number of common shares outstanding, plus the incremental shares that would have been outstanding upon the assumed exercise of all potentially dilutive stock options, warrants and convertible preferred stock, subject to anti-dilution limitations.

At December 31, 2008 and 2007, total options and warrants of 3,073,017 and 2,443,852, respectively, to purchase shares of common stock, were outstanding but were not included in the computation of diluted earnings per share as they were anti-dilutive as a result of net losses applicable to common shareholders during the periods.

At December 31, 2008 and 2007, options and warrants to purchase 25,000 and 2,540,567 shares of common stock with exercise prices below the market price, respectively, were outstanding but were not included in the computation of diluted earnings per share as they are anti-dilutive as a result of net losses during the period.

For both the three and six month periods ended December 31, 2008, common share equivalents of 1,779,755 related to the Convertible Note Payable were not included in the computation of diluted earnings per share as they were anti-dilutive as a result of net losses applicable to common shareholders.

Recent Accounting Pronouncements. In October 2008, the Financial Accounting Standards Board ("FASB") issued FSP No. 157-3, "Determining the Fair Value of a Financial Asset When the Market for That Asset Is Not Active" ("FSP 157-3"). FSP 157-3 clarifies the application of SFAS 157 in a market that is not active and provides an example to illustrate key considerations in determining the fair value of a financial asset when the market for that financial asset is not active. FSP 157-3 was effective for us on September 30, 2008 for all financial assets and liabilities recognized or disclosed at fair value in our Condensed Financial Statements on a recurring basis (at least annually).

In May 2008, the FASB issued SFAS No. 162, "The Hierarchy of Generally Accepted Accounting Principles." The statement is intended to improve financial reporting by identifying a consistent hierarchy for selecting accounting principles to be used in preparing financial statements that are presented in conformity with GAAP. Prior to the issuance of SFAS No. 162, GAAP hierarchy was defined in the American Institute of Certified Public Accountants ("AICPA") Statement on Auditing Standards (SAS) No. 69, The Meaning of Present Fairly in Conformity With Generally Accepted Accounting Principles. Unlike SAS No. 69, SFAS No. 162 is directed to the entity rather than the auditor. Statement No. 162 is effective 60 days following the SEC's approval of the Public Company Accounting Oversight Board Auditing amendments to AU Section 411, The Meaning of Present Fairly in Conformity with Generally Accepted Accounting Principles. SFAS No. 162 is not expected to have any material impact on the Company's results of operations, financial condition or liquidity.

Note 2. Discontinued Operations

In August 2008, we completed the spin-off of iBio. The Company has classified iBio as discontinued operations for the current and prior periods and the associated results of operations, financial position and cash flows are separately reported for all periods presented. As a result, we recognized an after-tax loss of $105 during the first quarter of the fiscal year ended 2009. iBio revenues from discontinued operations were $240 for the three months ended December 31, 2007, and $169, and $480 for the six months ended December 31, 2008 and 2007, respectively. The Company's loss from discontinued operations, net of taxes, was $246 for the three months ended December 31, 2007 and $105 and $518 for the six months ended December 31, 2008 and 2007, respectively.

INTEGRATED BIOPHARMA, INC. AND SUBSIDIARIES
NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
AS OF DECEMBER 31, 2008 AND JUNE 30, 2008 AND FOR THE
THREE AND SIX MONTHS ENDED DECEMBER 31, 2008 AND 2007
(in thousands, except share and per share amounts)

The net assets of iBio are classified as assets and liabilities related to discontinued operations in the Company's condensed consolidated balance sheet at June 30, 2008. The net assets were comprised of the following:

The Distribution was completed on August 18, 2008 and each shareholder of the Company received one share of iBio for each share the shareholder owned as of August 12, 2008. The Distribution should qualify as a tax-free reorganization under Section 355 of the Internal Revenue Code of 1986, as amended. The Separation and Distribution Agreement prohibits iBio from issuing more than 19,845,061 of additional shares of its common stock (representing the number of shares issued in connection with the Distribution) for the two years immediately following the effective date of the Distribution.

On August 19, 2008, the Company entered into a Conversion Agreement, whereby the Company caused approximately $5,209 of the intercompany debt to be contributed to additional paid in capital and used $2,700 of

INTEGRATED BIOPHARMA, INC. AND SUBSIDIARIES
NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
AS OF DECEMBER 31, 2008 AND JUNE 30, 2008 AND FOR THE
THREE AND SIX MONTHS ENDED DECEMBER 31, 2008 AND 2007
(in thousands, except share and per share amounts)

the intercompany debt to purchase approximately 1,266,706 common shares of iBio, representing 6% of the then outstanding common shares of iBio. The Company is carrying its investment in iBio of $2,700 on the cost basis. The Company owns 5.4% of the shares outstanding of iBio as of December 31, 2008.

In August 2008, the Company ceased allocating corporate overhead to iBio (formerly Biotechnologies Segment) and entered into a Transitional Services Agreement (the "TS Agreement") with iBiopharma, Inc. The transitional services agreement permits the Company to continue to provide certain corporate services in exchange for a management charge. The scope of these services is limited to legal, strategic financial planning and SEC reporting, and tax services by certain corporate employees of the Company. In exchange for these services, iBio will pay approximately $50 for certain financial and tax services over an estimated period of six months; the TS Agreement provides for a per annum fee of $100. In the three and six months ended December 31, 2008, the Company billed iBio approximately $25 and $37, respectively under the TS Agreement.

Note 3. Other Intangible Assets

Other intangible assets with indefinite lives are tested for impairment at the reporting unit level (operating segment or one level below an operating segment) on an annual basis and between annual tests if an event occurs or circumstances change that would more likely than not reduce the fair value of a reporting unit below its carrying value. Application of the impairment test requires judgment, including the identification of reporting units, assignment of assets and liabilities to reporting units, and determination of the fair value of each reporting unit.

Other intangible assets consist of intellectual property, trademarks, license fees, and unpatented technology. The carrying amount of other intangible assets as of December 31, 2008 and June 30, 2008 is as follows:

Amortization expense from continuing operations recorded on the intangible assets for the three and six months ended December 31, 2008 and 2007 was $60 and $119, and $92 and $200, respectively. Amortization expense is recorded on the straight-line method over periods ranging from 2 years to 20 years based on contractual or estimated lives and is included in selling and administrative expenses. Included in the Company's loss from discontinued operations is amortization expense of $56 for the three months ended December 31, 2007 and $33 and $126 related to iBio's intangible assets for the six months ended December 31, 2008 and 2007, respectively.

The estimated annual amortization expense for intangible assets for the five succeeding fiscal years is as follows:

INTEGRATED BIOPHARMA, INC. AND SUBSIDIARIES
NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
AS OF DECEMBER 31, 2008 AND JUNE 30, 2008 AND FOR THE
THREE AND SIX MONTHS ENDED DECEMBER 31, 2008 AND 2007
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Note 4. Inventories

Inventories are stated at the lower of cost or market using the first-in, first-out method and consist of the following as of December 31, 2008 and June 30, 2008:

Note 5. Property and Equipment

Property and equipment consists of the following as of:

Note 6. Notes Payable and Convertible Note Payable – CD Financial, LLC

INTEGRATED BIOPHARMA, INC. AND SUBSIDIARIES
NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
AS OF DECEMBER 31, 2008 AND JUNE 30, 2008 AND FOR THE
THREE AND SIX MONTHS ENDED DECEMBER 31, 2008 AND 2007
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On February 19, 2008, the Company entered into two Securities Purchase Agreements (the "SPAs") relating to a private placement of securities with two investors, one of whom is an affiliate of Carl DeSantis, a director of the Company, which resulted in gross proceeds of $17,337 to the Company. The private placement involved the sale of (i) 6,000 shares of newly designated redeemable Series C Convertible Preferred Stock (the “Series C Preferred”) with a stated value of $1,000 per share (see Note 10(d) Series C Redeemable Convertible Preferred Stock), (ii) $4,500 in principal amount of 9.5% Convertible Note Payable (the “Convertible Note Payable”), (iii) $7,000 in principal amount of 8.0% Notes Payable, which was amended on October 14, 2008 (the “Notes Payable”) and (iv) 200,000 shares of the Company’s common stock. The Company also recorded $218 of deferred financing costs associated with the two SPA's, $130 of such deferred financing costs were netted against the gross proceeds received. These costs were allocated to the each of the components of the transaction, based on the relative fair values and are amortized based on the terms of the component of the transaction for which the costs were allocated to respectively. As of June 30, 2008 and December 31, 2008, the Company had deferred financing costs remaining of $113 and $55, respectively, which is to be amortized to interest expense over one to three years. The Notes Payable and the Convertible Note Payable are secured by a pledge of substantially all of our assets.

The Company has accreted $54 and $1,137 for the six months ended December 31, 2008 for the Series C Preferred Stock Dividend and for the acceleration of the deemed dividend from the beneficial conversion feature of the Series C Preferred Stock, respectively (See Note 10(d) Series C Redeemable Convertible Preferred Stock). Such amounts are included in the accompanying Condensed Consolidated Statement of Operations.

(a) Convertible Note Payable - CD Financial, LLC, a related party, provided gross proceeds of $7,500, in exchange for 3,000 shares of Series C Preferred Stock and a Convertible Note Payable. The Convertible Note Payable has a principal amount of $4,500 with an annual interest rate of 9.5% and matures on February 21, 2011. The Company allocated the proceeds of $4,500 and the discount of $98 based the relative fair value of the Convertible Note Payable in connection with this transaction. The Company is amortizing to interest expense the discount applied to the Convertible Note Payable over the term of the note. The Company recorded a beneficial conversion feature, in accordance with EITF 00-27, on the Convertible Note Payable of $715 to be accreted over the three-year period until maturity or the redemption of the Convertible Note Payable. For the three and six months ended December 31, 2008, included in interest expense in the accompanying Condensed Consolidated Statement of Operations, are $65 and $130 related to the accretion of the discount and accretion of the beneficial

INTEGRATED BIOPHARMA, INC. AND SUBSIDIARIES
NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
AS OF DECEMBER 31, 2008 AND JUNE 30, 2008 AND FOR THE
THREE AND SIX MONTHS ENDED DECEMBER 31, 2008 AND 2007
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conversion feature on the Convertible Notes, respectively. As of December 31, 2008 and June 30, 2008, the unpaid discount which was allocated as of the date of the transaction based on the gross proceeds provided by CD Financial, LLC was $163. This is included in accrued expenses in the accompanying Condensed Consolidated Balance Sheet. Also, in accordance with the Convertible Note Payable, the Company will issue and deliver to CD Financial LLC, for no additional consideration, 50,000 shares of Common Stock, on a quarterly basis in arrears, commencing with the three-month anniversary of the issuance date, until the Convertible Note has been repaid in full, after which the Company's obligations to issue shares of Common Stock will no longer be applicable. As of December 31, 2008, the Company had accrued and unpaid interest of approximately $36, for the Convertible Note Payable in the accompanying Condensed Consolidated Balance Sheet.

The beneficial conversion feature for the Convertible Note Payable will be accreted using the effective interest rate method. The Convertible Note Payable may be converted, at any time and at the holder’s option, into shares of our common stock based on a conversion price as set out in the Convertible Note Payable. The conversion price is a formula that bases the conversion price on the greater of (i) 90% of the average Volume Weighted Average Price (the "VWAP") market price of our common stock for 20 trading days immediately preceding the conversion date and (ii) $2.00, subject to adjustment in the event of a stock dividend, stock split or combination, reclassification or similar event and upon certain issuances below the conversion price. We have the option to prepay the Convertible Note Payable at any time.

(b) Notes Payable, provided proceeds of $9,837, which includes a discount of $163 in exchange for 3,000 shares of Series C Preferred Stock, Notes Payable and 200,000 shares of the Company’s common stock. The Company allocated the proceeds from the $10,000 and the discount of $163 to the components of the transaction based the relative fair value of the Notes Payable, the Series C Preferred Stock and the Company’s common stock in connection with this transaction.

On October 14, 2008, the Company and the Notes Payable holders amended the SPA to extend the maturity from February 21, 2009 to November 15, 2009. In consideration for extending the maturity of the Notes Payable, the Notes Payable holders will forgo the 200,000 shares of Common Stock as additional interest and the Company will (i) grant a 11.5% premium on the principal, thus aggregating a principal balance due of $7,805 and certain other amounts payable under the Notes Payable, if any, (ii) certain new covenants will be applicable to the Company effective October 14, 2008, (iii) the Company shall issue warrants to purchase 500,000 shares of the Company’s Common Stock, with a five year term and an exercise price of $0.80 per share, and (iv) the registration of the resale of the shares of the Company’s Common Stock for which the warrants are exercisable. Since the October 14, 2008 amendment significantly modified the terms of the original Notes Payable, the Company has accounted for the amendment as an extinguishment of the original Notes Payable and issuance of new Notes Payable, per EITF Issue No. 96-19, “Debtor’s Accounting for a Modification or Exchange of Debt Instruments.” As a result, the Company accelerated the amortization of the remaining discount of $178 and prepaid financing costs of $32 applied to the

original Notes Payable to interest expense as a result of the extinguishment. Furthermore, the Company reversed the accrual of additional consideration of $208 related to the 200,000 shares of the Company's common stock.

The amended Notes Payable of $7,000 bear an interest rate of 8.0% and will mature on November 15, 2009. The Company is accreting the premium of $805 over the term of the amendment, using the effective interest method, which has resulted in additional interest expense for the three and six months ended December 31, 2008 of $152. The warrants issued with the amended Notes Payable were valued at a fair value of $169 using the Black-Scholes option pricing model as of the issuance date. The Company used the following assumptions to calculate the fair value of the warrants; risk free interest rate of 3.0%, expected volatility of 75.8%, a term of 5 years and a dividend yield of zero. The discount to the amended Notes Payable for the warrants which are being accreted using the effective interest method, has resulted in additional interest expense for the three and six months ended December 31, 2008 of $33. The Company also recorded an additional $10 of deferred financing costs as a result of the issuance of the

INTEGRATED BIOPHARMA, INC. AND SUBSIDIARIES
NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
AS OF DECEMBER 31, 2008 AND JUNE 30, 2008 AND FOR THE
THREE AND SIX MONTHS ENDED DECEMBER 31, 2008 AND 2007
(in thousands, except share and per share amounts)

amended Notes Payable. The amended Notes Payable agreement requires the Company to register for resale the shares of Common Stock for which the warrants are exercisable prior to 90 days after the closing date of October 14, 2008. The Company had not registered the warrants as of December 31, 2008. The failure to register the warrants results in a default payment of the greater of $8 or 2.0% of the market price as of the date on which the registration default occurred multiplied by the number of unregistered warrants. As of the date of the filing, the Company has not registered the securities. The Company will incur a de-minimis penalty amount in the third quarter of the fiscal year ending June 30, 2009. The Company is amortizing to interest expense the deferred financing costs using the effective interest method. The amount amortized related to the amended Notes Payable for the three and six months ended December 31, 2008 is $2.

For the three and six months ended December 31, 2008, included in interest expense in the accompanying Consolidated Statement of Operations, is $448 and $637 related to the accretion of the discount on the original and amended Notes Payable. As of December 31, 2008, the Company had accrued and unpaid interest of approximately $47, for the amended Notes Payable in the accompanying Condensed Consolidated Balance Sheet.

As of December 31, 2008 the Company is in default of the covenants of the Notes Payable. The Company is currently working with the holders to obtain a waiver for the default of the covenants; however at this time the Company has not obtained such waiver.

Note 7. Significant Risks and Uncertainties

(a) Concentrations of Credit Risk-Cash. The Company maintains balances at several financial institutions. Deposits at each institution are insured by the Federal Deposit Insurance Corporation up to $250 through December 31, 2009. As of December 31, 2008, the Company had uninsured cash balances of approximately $207 on deposit with JP Morgan Chase. The FDIC is temporarily insuring deposits up to $250,000 at financial institutions through December 31, 2009. Additionally, JP Morgan Chase is participating in the FDIC's Transaction Account Guarantee Program, whereby all non-interest bearing checking accounts (including accounts with interest rates less than 0.50%) are fully guaranteed by the FDIC for the entire amount through December 31, 2009.

(b) Concentrations of Credit Risk-Receivables. The Company routinely assesses the financial strength of its customers and, based upon factors surrounding the credit risk of its customers, establishes an allowance for uncollectible accounts and, as a consequence, believes that its accounts receivable credit risk exposure beyond such allowances is limited. The Company does not require collateral in relation to its trade accounts receivable credit risk. The amount of the allowance for uncollectible accounts and other allowances was $190 and $134 at December 31, 2008 and June 30, 2008, respectively.

(c) Major Customers. For the three months ended December 31, 2008 and 2007 approximately 72.1% and approximately 68.4%, respectively, of revenues were derived from three customers. For the six months ended December 31, 2008 and 2007 approximately 70.1% and approximately 67.1%, respectively, of revenues were derived from three customers. Accounts receivable from these customers represented approximately 52.9% of total accounts receivable as of December 31, 2008. The loss of any of these customers would have an adverse affect on the Company's operations. Major customers are those customers who account for more than 10% of net sales.

(d) Other Business Risks. The Company insures its business and assets against insurable risks, to the extent that it deems appropriate, based upon an analysis of the relative risks and costs. The Company believes that the risk of loss from non-insurable events would not have a material adverse effect on the Company's operations as a whole.

The raw materials used by the Company are primarily commodities and agricultural-based products. Raw materials used by the Company in the manufacture of its Nutraceutical products are purchased from independent suppliers. Raw materials are available from numerous sources and the Company believes that it will continue to obtain adequate supplies.

Of the employees located in the Company's New Jersey facility, approximately 54% the employees are covered by a union contract, which expires August 31, 2010.

INTEGRATED BIOPHARMA, INC. AND SUBSIDIARIES
NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
AS OF DECEMBER 31, 2008 AND JUNE 30, 2008 AND FOR THE
THREE AND SIX MONTHS ENDED DECEMBER 31, 2008 AND 2007
(in thousands, except share and per share amounts)

Note 8. Commitments and Contingencies

(a) Leases

Related Party Leases. Warehouse and office facilities are leased from Vitamin Realty Associates, L.L.C., a limited liability company, which is 90% owned by the Chairman of the Company's Board of Directors, a director and majority shareholder and certain family members and 10% owned by an employee of the Company. The lease provides for minimum annual rental payment of $324 through May 31, 2015 plus increases in real estate taxes and building operating expenses. On July 1, 2004, the Company leased an additional 24,810 square feet of warehouse space on a month-to month basis. Rent expense for the three and six months ended December 31, 2008 and 2007 on these leases were $183 and $179, respectively, and are included in both cost of sales and selling and administrative expenses in the accompanying Condensed Consolidated Statements of Operations. At December 31, 2008 and June 30, 2008 the Company had an outstanding obligation of $278 and $224 included in accounts payable in the accompanying Consolidated Balance Sheet.

Other Lease Commitments. The Company has entered into certain non-cancelable operating lease agreements expiring up through May 31, 2015, related to office and warehouse space, equipment and vehicles. Total rent expense, including real estate taxes and maintenance charges, was approximately $390 and $440 for the three months ended December 31, 2008 and 2007, respectively; and $844 and $860 for the six months ended December 31, 2008 and 2007, respectively. Rent expense is stated net of sublease income of approximately $9 for the three months ended December 31, 2008 and 2007; and $17 and $25 for the six months ended December 31, 2008 and 2007, respectively. This is included in both cost of sales and selling and administrative expenses in the accompanying Condensed Consolidated Statements of Operations.

The minimum rental commitment for long-term non-cancelable leases is as follows:

(c) Paxis Purchase Agreement. In connection with the Company's acquisition of Paxis from Trade Investment Services, LLC ("TIS"), which funded Paxis' and Natex's development, TIS has the right to receive twenty-five (25%) of the after-tax profits of Paxis until TIS has received an additional $49.5 million. At this time, the Company is unable to estimate the amount or timing of any potential contingent payments.

E. Gerald Kay, the Chairman of the Company's Board of Directors, a director and majority shareholder of INBP; Robert Kay, the brother of E. Gerald Kay, shareholder of INB; and Carl DeSantis, a director and shareholder of INB, each own one-third (1/3) of the equity of TIS.

INTEGRATED BIOPHARMA, INC. AND SUBSIDIARIES
NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
AS OF DECEMBER 31, 2008 AND JUNE 30, 2008 AND FOR THE
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(d) Consulting Agreements.

Effective July 1, 2008, the Company entered into a consulting agreement, pursuant to which the consultant is to provide consulting and specialized services to the Company in the area of finance, acquisition of product lines, refinancing of existing debt and capital raising under the direction of the Company, including for any company in which the Company has an ownership interest. In connection with the agreement, the Company issued 100,000 shares of the Company's common stock associated with the three year consulting agreement (See Note 10. Equity Transactions).

Effective July 1, 2008, the Company entered into a consulting agreement with Jeffrey R. Leach (an employee of the Company as of the date of the agreement) its current President and Chief Executive Officer, pursuant to the consulting agreement, Mr. Leach is to provide consulting and specialized services to the Company in the area of finance, acquisition of product lines, refinancing of existing debt and capital raising under the direction of the Company, including for any company in which the Company has an ownership interest. In connection with the agreement, the Company issued 250,000 shares of the Company's common stock associated with the three year consulting agreement (See Note 10. Equity Transactions).

Note 9. Related Party Transactions

The Company is a party to a verbal consulting agreement with Eugene Kay, a former employee of the Company and a brother of E. Gerald Kay, the Chairman of the Company's Board of Directors, a director and majority shareholder of the Company. This agreement provides for consulting services on a month-to-month basis for $1 per month. The total consulting expense recorded for the three and six months ended December 31, 2008 and 2007 was $3 in each period. The Company was party to another consulting agreement with EVJ, LLC, a limited liability company controlled by Robert Kay, a shareholder of the Company, the Chairman of its subsidiary, InB: Paxis, and a brother of E. Gerald Kay and Eugene Kay. This agreement was assumed by and became a liability of the Company as a part of the Company's acquisition of Paxis Pharmaceuticals Inc. in fiscal year ended June 30, 2004. This agreement was terminated in during the first quarter of fiscal year 2009. The total consulting expense under this agreement was $15 and $30 for each of the three month period ended December 31, 2007 and $15 and $60 for the six month period ended December 31, 2008 and 2007, respectively.

See Note 2 – Discontinued Operations for related party transactional service agreement with iBioPharma, Inc.

See Note 6(a) – Notes Payable and Convertible Note Payable – CD Financial, LLC for related party securities transactions.

See Note 8(a) - Leases for related party lease transactions.

See Note 8(d) – Consulting Agreements for related party consulting agreements.

Note 10. Equity Transactions

(a) Stock Option Plan and Warrants. During the three and six months ended December 31, 2008, there was 1,000,000 stock options authorized by the Board of Directors and issued to Company employees, and warrants to purchase 500,000 shares of common stock at $0.80 in connection with the amended Notes Payable agreement (See Note 6(b) Notes Payable). During the three and six months ended December 31, 2007 the Company issued stock options of 690,800 and 700,800; respectively. There were no warrants issued in the three and six month periods ended December 31, 2007. During the three and six months ended December 31, 2008 and 2007, the Company has incurred stock compensation expense of $304 and $869, and $777 and $1,010; respectively. Included is stock compensation related to the Biotechnologies Segment, of $4 for the six months ended December 31,

2008, and $14 and $28 for the three and six months ended December 31, 2007, respectively.