

Edgar Filing: LANNETT CO INC - Form 10KSB

LANNETT CO INC  
Form 10KSB  
September 26, 2002

U.S. SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549

FORM 10-KSB

(Mark One)

ANNUAL REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT  
OF 1934  
FOR THE FISCAL YEAR ENDED JUNE 30, 2002

OR

TRANSITION REPORT UNDER SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE  
ACT OF 1934  
FOR THE TRANSITION PERIOD FROM \_\_\_\_\_ TO \_\_\_\_\_

Commission File No. 0-9036

LANNETT COMPANY, INC.  
(Name of small business issuer in its charter)

STATE OF DELAWARE  
State of Incorporation

23-0787-699  
I.R.S. Employer I.D. No.

9000 STATE ROAD  
PHILADELPHIA, PENNSYLVANIA 19136  
(215) 333-9000  
(Address of principal executive offices and telephone number)

Securities registered under Section 12(b) of the Exchange Act:  
NONE

Securities registered under Section 12(g) of the Exchange Act:  
COMMON STOCK, \$.001 PAR VALUE  
(Title of class)

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

Yes X No  
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Check if there is no disclosure of delinquent filers in response to  
Item 405 of Regulation S-B contained in this form, and no disclosure will be  
contained, to the best of registrant's knowledge, in definitive proxy or  
information statements incorporated by reference in Part III of this Form 10-KSB  
or any amendment to this Form 10-KSB.

The issuer had net sales of \$25,126,214 for the fiscal year ended  
June 30, 2002.

As of September 3, 2002, the aggregate market value of the voting  
stock held by non-affiliates was approximately \$116,456,000 computed by  
reference to the closing price of the stock on the American Stock Exchange.

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As of September 3, 2002, there were 13,263,838 shares of the issuer's common stock, \$.001 par value, outstanding.

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Exhibit Index on Page 40

## PART I

### ITEM 1. DESCRIPTION OF BUSINESS

#### GENERAL.

Lannett Company, Inc. (the "Company") was incorporated in 1942 under the laws of the Commonwealth of Pennsylvania. In 1991, the Company merged into Lannett Company, Inc., a Delaware corporation. The sole purpose of the merger was to reincorporate the Company as a Delaware corporation. The Company develops, manufactures, packages, markets and distributes pharmaceutical products sold under generic chemical names. In addition, the Company contract manufactures and private labels pharmaceutical products for other companies. Currently, the Company manufactures only solid oral dosage forms, including tablets and capsules; but the Company is pursuing partnerships and research contracts for the development and production of other dosage forms, including liquids and injectable products.

The Company's headquarters, administrative offices, quality control laboratory, manufacturing and production facilities, consisting of approximately 31,000 square feet, are located at 9000 State Road, Philadelphia, Pennsylvania. In December 1997, the Company entered into a three-year and three-month lease for a 23,500 square foot facility located at 500 State Road, Bensalem Bucks County, Pennsylvania. The leased facility is located approximately 1.5 miles from its headquarters in Philadelphia. In January 2001, the Company extended this lease through April 30, 2004. This facility houses research, development, warehousing and distribution operations.

#### PRODUCTS.

As of the date of this filing, the Company manufactured and/or distributed fifteen products:

NAME OF PRODUCT	MEDICAL INDICATION	EQUIVALENT BRAND NAME PRODUCT
1.) Butalbital, Aspirin and Caffeine Capsules	Migraine Headache	Fiorinal(R)
2.) Butalbital, Aspirin, Caffeine with Codeine Capsules	Migraine Headache	Fiorinal(R) with Codeine
3.) Digoxin .125 mg Tablets	Heart Failure	Lanoxin(R)
4.) Digoxin .25 mg Tablets	Heart Failure	Lanoxin(R)
5.) Primidone 50 mg Tablets	Epilepsy	Mysoline(R)
6.) Primidone 250 mg Tablets	Epilepsy	Mysoline(R)
7.) Dicyclomine 10 mg Capsules	Irritable Bowels	Bentyl(R)
8.) Dicyclomine 20 mg Tablets	Irritable Bowels	Bentyl(R)
9.) Acetazolamide 250 mg Tablets	Glaucoma	Diamox(R)
10.) Prednisolone 5 mg Tablets	Antibacterial steroid	Not applicable
11.) Diphenoxylate with Atropine Sulfate Tablets	Diarrhea	Lomotil(R)
12.) Methylprednisolone Tablets	Steroid	Medrol(R)

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13.) Isoniazid 300 mg Tablets	Tuberculosis	Not applicable
14.) Pseudoephedrine 30 mg Tablets	Allergies	Sudafed(R)
15.) Guaifenesin with Ephedrine Tablets	Allergies	Not applicable

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Additional products are also currently under development. Five of these products have been redeveloped and submitted to the Food and Drug Administration ("FDA") for supplemental approval. The remainder of the products in development represent either previously approved Abbreviated New Drug Applications ("ANDA's") which the Company is planning to reintroduce, or new formulations which the Company will submit ANDA's for FDA approval. The Company has also begun solicitation of quotes from outside contract development companies to supplement the Company's internal research and development efforts. Since the Company has no control over the FDA review process, management is unable to anticipate whether or when it will be able to begin producing and shipping additional products.

### RAW MATERIALS.

The raw materials used by the Company in the manufacture of pharmaceutical products consist of pharmaceutical chemicals in various forms, which are available from various sources. FDA approval is required in connection with the process of selecting active ingredient suppliers. One supplier accounted for approximately 30% of the Company's raw material purchases in Fiscal 2002. That supplier and an additional supplier accounted for approximately 27% and 24% of the Company's raw material purchases in Fiscal 2001. The raw materials purchased from these suppliers are available from a number of vendors.

### DISTRIBUTION.

The Company sells its pharmaceutical products primarily to wholesalers, distributors, warehousing chains, retail chains and other pharmaceutical companies. Sales of the Company's pharmaceutical products are made on an individual order basis. Two customers accounted for approximately 22% and 19%, respectively, of net sales in Fiscal 2002. One of these customers accounted for approximately 24% of net sales in Fiscal 2001. As the Company introduces additional products and opens new customer accounts, it expects to broaden its customer base.

### COMPETITION.

The manufacture and distribution of generic pharmaceutical products is a highly competitive industry. Competition is primarily based on quality, price and service. The Company intends to compete primarily on this basis, as well as flexibility, availability of inventory, and by the fact that the Company's products are only available from a limited number of competitors. The modernization of its facilities, hiring of experienced staff, and implementation of inventory and quality control programs have improved the Company's competitive position over the past five years.

GOVERNMENT REGULATION.

Pharmaceutical manufacturers are subject to extensive regulation by the federal government, principally by the FDA and the Drug Enforcement Agency ("DEA"), and, to a lesser extent, by other federal regulatory bodies and state governments. The Federal Food, Drug and Cosmetic Act, the Controlled Substance Act and other federal statutes and regulations govern or influence the testing, manufacture, safety, labeling, storage, record keeping, approval, pricing, advertising and promotion of the Company's generic drug products. Noncompliance with applicable regulations can result in fines, recall and seizure of products, total or partial suspension of production, personal and/or corporate prosecution and debarment, and refusal of the government to approve new drug applications. The FDA also has the authority to revoke previously approved drug products.

FDA approval is required before any prescription drug can be marketed. The approval procedures are generally quite burdensome. A new drug is one not generally recognized by qualified experts as safe and effective for its intended use. New drugs are typically developed and submitted to the FDA by companies expecting to brand the product and sell it as a new medical treatment. The FDA review process for new drugs is very extensive; and it requires the submitting entity to make substantial investments in researching and testing the drug candidate. However, less burdensome approval procedures may be used for generic equivalents. Typically, the investment by a generic drug manufacturer in developing and submitting to the FDA an application for a generic drug is much less costly. There are currently three ways to obtain FDA approval of a new drug.

NEW DRUG APPLICATIONS ("NDA"). Unless one of the two procedures discussed in the following paragraphs is available, a manufacturer must conduct and submit to the FDA complete clinical studies to establish a drug's safety and efficacy.

ABBREVIATED NEW DRUG APPLICATIONS ("ANDA"). An ANDA is similar to an NDA, except that the FDA waives the requirement of complete clinical studies of safety and efficacy, although it may require bioavailability and bioequivalence studies. This process normally takes approximately 18 months. "Bioavailability" indicates the rate of absorption and levels of concentration of a drug in the bloodstream needed to produce a therapeutic effect. "Bioequivalence" compares one drug product with another, and when established, indicates that the rate of absorption and the levels of concentration of a generic drug in the body are within prescribed statistical limits to those of a previously approved equivalent drug. Under the Drug Price Act, an ANDA may be submitted for a drug on the basis that it is the equivalent of an approved drug, regardless of when such other drug was approved. The Drug Price Act, in addition to establishing a new ANDA procedure, created statutory protections for approved brand name drugs. Under the Drug Price Act, an ANDA for a generic drug may not be made effective until all relevant products and use patents for the equivalent brand name drug have expired or have been determined to be invalid. Prior to enactment of the Drug Price Act, the FDA gave no consideration to the patent status of a previously approved drug. Additionally, the Drug Price Act extends for up to five years the term of a product or use patent covering a drug to compensate the patent holder for the reduction of the effective market life of a patent due to federal regulatory review. With respect to certain drugs not covered by patents, the Drug Price Act sets specified time periods of two to ten years during which ANDA's for generic drugs cannot become effective or, under certain circumstances, cannot be filed if the equivalent brand name drug was approved after December 31, 1981.

PAPER NEW DRUG APPLICATIONS ("PAPER NDA"). For drugs which are identical to a drug first approved after 1962, a prospective manufacturer need not go through the full NDA procedure, but instead may demonstrate safety and efficacy by reliance on published literature and reports, and must also submit, if the FDA so requires, bioavailability or bioequivalence data illustrating that the generic drug formulation produces, within an acceptable range, the same effects as the previously approved equivalent drug. Because published literature to support the safety and efficacy of post-1962 drugs may not be generally available, this procedure is of limited utility to generic drug manufacturers. Moreover, the utility of Paper NDA's has been even further diminished by the recently broadened availability of the abbreviated new drug application as described above.

Among the requirements for new drug approval is the requirement that the prospective manufacturer's methods conform to the FDA's current good manufacturing practices ("CGMP Regulations"). The CGMP Regulations must be followed at all times during which the approved drug is manufactured. In complying with the standards set forth in the CGMP regulations, the Company must continue to expend time, money and effort in the areas of production and quality control to ensure full technical compliance. Failure to comply with the CGMP regulations risks possible FDA action such as the seizure of noncomplying drug products or, through the Department of Justice, enjoining the manufacture of such products.

The Company is also subject to federal, state and local laws of general applicability, such as laws regulating working conditions, and, to the extent that its business operations entail the generation, storage, transportation or discharge of items that may be considered hazardous substances, hazardous waste or environmental contaminants, the Company may be subject to various federal, state and local environmental protection laws and regulations. The Company monitors its compliance with all environmental laws. Any compliance costs, which may be incurred, are contingent upon the results of future site monitoring and will be charged against operations when incurred. The Company incurred no monitoring costs during the years ended June 30, 2002 and 2001.

#### RESEARCH AND DEVELOPMENT.

During Fiscal 2002 and Fiscal 2001, the Company incurred research and development costs of approximately \$1,749,000 and \$1,403,000, respectively.

#### EMPLOYEES.

The Company currently employs 135 employees, all of whom are full-time.

#### ITEM 2. DESCRIPTION OF PROPERTY

The Company's headquarters, administrative offices, quality control laboratory, manufacturing and production facilities are located at 9000 State Road, Philadelphia, Pennsylvania. This facility is approximately 31,000 square feet, located on four and one half (4-1/2) acres. The Company had increased its warehousing activities beyond the capacity of its current facility. As a result, in December 1997, the Company entered into a three-year and three-month lease for a 23,500

square foot facility located at 500 State Road, Bensalem Bucks County, Pennsylvania. The leased facility is located approximately 1.5 miles from its headquarters in Philadelphia. In January 2001, the Company extended this lease through April 30, 2004. This facility houses research, development, warehousing and distribution operations.

ITEM 3. LEGAL PROCEEDINGS

REGULATORY PROCEEDINGS.

The Company is engaged in an industry which is subject to considerable government regulation relating to the development, manufacturing and marketing of pharmaceutical products. Accordingly, incidental to its business, the Company periodically responds to inquiries or engages in administrative and judicial proceedings involving regulatory authorities, particularly the FDA and the DEA.

EMPLOYEE CLAIMS.

A claim of retaliatory discrimination has been filed by a former employee with the Pennsylvania Human Relations Commission ("PHRC") and the Equal Employment Opportunity Commission ("EEOC"). The Company has denied liability in this matter. The PHRC has made a determination that the complaint against the Company should be dismissed because the facts do not establish probable cause of the allegations of discrimination. The matter is still pending before the EEOC. At this time, management is unable to estimate a range of loss, if any, related to this action. Management believes that the outcome of this claim will not have a material adverse impact on the financial position or results of operations of the Company.

Additionally, two separate claims of discrimination have been filed against the Company with the PHRC and the EEOC. The Company was notified of the Complaints in June 2001 and July 2001, respectively. The Company has filed answers with the PHRC and EEOC denying the allegations. The PHRC and the EEOC are investigating the claims pursuant to their normal procedures. At this time, management is unable to estimate a range of loss, if any, related to these actions. Management believes that the outcomes of these claims also will not have material adverse impacts on the financial position or results of operations of the Company.

DES CASES

The Company is currently engaged in several civil actions as a co-defendant with many other manufacturers of Diethylstilbestrol ("DES"), a synthetic hormone. Prior litigation established that the Company's pro rata share of any liability is less than one-tenth of one percent. The Company was represented in many of these actions by the insurance company with which the Company maintained coverage during the time period that damages were alleged to have occurred. The insurance company denied coverage of actions filed after January 1, 1992. With respect to these actions, the Company paid nominal damages or stipulated to its pro rata share of any liability. The Company has either settled or is currently defending over 500 such claims. At this time,

management is unable to estimate a range of loss, if any, related to these actions. Management believes that the outcome of these cases will not have a material adverse impact on the financial position or results of operations of the Company.

CONTRACT DISPUTE

The Company was engaged in a civil lawsuit as the plaintiff based on a contract dispute regarding raw material for use in one of the Company's new products in development. The lawsuit was initiated after a chemical supplier failed to supply the Company with raw material for its manufacturing process, despite the existence of a signed five-year supply contract. The Company alleged that the breach of contract delayed the introduction of one of its products into the marketplace. The Company and the defending party settled the suit prior to trial. The Company received approximately \$1.5 million in First Quarter Fiscal 2001. The Company incurred approximately \$305,000 in legal fees relating to the lawsuit in Fiscal 2000. These fees were expensed to operations as they were incurred.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

No matters have been submitted to a vote of the Company's security holders during the quarter ended June 30, 2002.

PART II

ITEM 5. MARKET FOR COMMON EQUITY AND RELATED STOCKHOLDER MATTERS

MARKET INFORMATION.

On April 15, 2002, the Company's common stock began trading on the American Stock Exchange. Prior to this, the Company's common stock traded in the over-the-counter market through the use of the inter-dealer "pink-sheets" published by Pink Sheets LLC. The following table sets forth certain information with respect to the high and low daily closing prices of the Company's common stock during Fiscal 2002 and 2001 as quoted by the American Stock Exchange (on and after April 15, 2002) and Pink Sheets LLC (prior to April 15, 2002). Such quotations reflect inter-dealer prices without retail mark-up, markdown or commission and may not represent actual transactions.

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FISCAL YEAR ENDED JUNE 30, 2002	
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	HIGH ----
First quarter.....	\$1.99
Second quarter.....	\$4.04
Third quarter.....	\$5.65

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Fourth quarter..... \$12.00

FISCAL YEAR ENDED JUNE 30, 2001  
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	HIGH
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First quarter.....	\$0.63
Second quarter.....	\$0.81
Third quarter.....	\$0.75
Fourth quarter.....	\$1.25

HOLDERS

The number of holders of record of the Company's common stock as of August 10, 2002 was 385.

DIVIDENDS.

The Company did not pay any cash dividends in Fiscal 2002 or 2001. The Company intends to use all available funds for the Company's working capital and does not anticipate paying cash dividends in the foreseeable future.

ITEM 6. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS.

In addition to historical information, this Form 10-KSB contains forward-looking information. The forward-looking information is subject to certain risks and uncertainties that could cause actual results to differ materially from those projected in the forward-looking statements. Important factors that might cause such a difference include, but are not limited to, those discussed in the following section entitled "Management's Discussion and Analysis of Financial Condition and Results of Operations." Readers are cautioned not to place undue reliance on these forward-looking statements, which reflect management's analysis only as of the date of this Form 10-KSB. The Company undertakes no obligation to publicly revise or update these forward-looking statements to reflect events or circumstances which arise later. Readers should carefully review the risk factors described in other documents the Company files from time to time with the Securities and Exchange Commission, including the Quarterly reports on Form 10-QSB to be filed by the Company in Fiscal 2002, and any Current Reports on Form 8-K filed by the Company.

RESTATEMENT

The Company has corrected and restated its Fiscal 2001 financial statements due to the correction of an error resulting from the improper deferral of legal fees at June 30, 2000 incurred associated with the favorable settlement of a lawsuit. The effect of the restatement as of and for the year ended June 30, 2001 was to increase other income and previously reported net income by \$305,128, or \$.02 per diluted share. This impact is reflected in the reported results herein.

CRITICAL ACCOUNTING POLICIES



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The discussion and analysis of our financial condition and results of operations are based upon our consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States of America. The preparation of these financial statements requires us to make estimates and judgments that affect the reported amount of assets and liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities at the date of our financial statements. Actual results may differ from these estimates under different assumptions or conditions.

Critical accounting policies are defined as those that are reflective of significant judgments and uncertainties, and potentially result in materially different results under different assumptions and conditions. We believe that our critical accounting policies include those described below. For a detailed discussion on the application of these and other accounting policies, see Note 1 in the Notes to the Consolidated Financial Statements included herein.

### REVENUE RECOGNITION

The Company recognizes revenue when its products are shipped. Under a contract in which product development occurs, the Company recognizes revenue when services are

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rendered. There are no inventory consignments held at customers' locations. Provisions for estimated rebates, chargebacks, returns and other adjustments are provided for in the period the related sales are recorded. If the historical data the Company uses to calculate these estimates does not accurately approximate future activity, its net sales, gross profit, net income and earnings per share could decrease. However, management believes that these estimates are reasonable based upon historical experience and current conditions.

### ACCOUNTS RECEIVABLE

The Company performs ongoing credit evaluations of its customers and adjusts credit limits based upon payment history and the customer's current credit worthiness, as determined by a review of their current credit information. The Company continuously monitors collections and payments from its customers and maintains a provision for estimated credit losses based upon historical experience and any specific customer collection issues that have been identified. While such credit losses have historically been within the Company's expectations and the provisions established, the Company cannot guarantee that it will continue to experience the same credit loss rates that it has in the past.

### INVENTORIES

The Company values its inventory at the lower of cost or market and regularly reviews inventory quantities on hand and records a provision for excess and obsolete inventory based primarily on estimated forecasts of product demand and production requirements. The Company's estimates of future product demand may prove to be inaccurate, in which case it may have understated or overstated the provision required for excess and obsolete inventory. In the future, if the Company's inventory is determined to be overvalued, the Company would be required to recognize such costs in cost of goods sold at the time of such determination. Likewise, if inventory is determined to be undervalued, the

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Company may have recognized excess cost of goods sold in previous periods and would be required to recognize such additional operating income at the time of sale.

### RESULTS OF OPERATIONS - FISCAL 2002 TO FISCAL 2001.

Net sales in Fiscal 2002 increased by 108% to \$25,126,214 from net sales of \$12,090,993 for Fiscal 2001. Sales increased as a result of additions to the Company's prescription line of products, including Primidone 50 mg tablets, first marketed in May 2001, Prednisolone tablets, first marketed in October 2001, Butalbital with Aspirin, Caffeine and Codeine Phosphate capsules, first marketed in December 2001, and Isoniazid tablets, first marketed in January 2002. Additionally, sales increased due to improved marketing activities, new customer accounts, favorable market conditions, increased unit sales, and increased unit revenues on a portion of the Company's niche line of products. In the last quarter of Fiscal 2001, one of the Company's competitors suspended production and distribution of a generic product which the Company continued to produce and market. Consequently, the Company was able to increase its sales output to meet the unchanged demand for the item. The Company increased the total revenue earned related to the product, thereby increasing the total sales for the period compared to the prior period. The increase in prescription sales was offset by a decrease in over-the-counter (OTC) product sales, due to increased competition. Prescription sales increased by approximately \$14,597,000 for Fiscal 2002 compared to Fiscal 2001. OTC sales decreased by approximately

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\$1,562,000 for Fiscal 2002 compared to Fiscal 2001. As the Company introduces additional products, it expects to continue increasing Rx product sales.

Cost of sales in Fiscal 2002 increased by 30% to \$8,452,677, from \$6,534,764 in Fiscal 2001. The cost of sales increase is due to an increase in direct variable costs and certain indirect overhead costs as a result of the increase in sales volume, and related production activities. These costs include raw materials, labor and benefits expenses, depreciation expense, and manufacturing and laboratory supplies. Gross profit margins for Fiscal 2002 and Fiscal 2001 were 66% and 46%, respectively. The increase in the gross profit percentage is due to a more profitable product sales mix, higher absorption of fixed overhead and production costs, and improved unit profit margins on the Company's niche line of products.

Research and development expenses in Fiscal 2002 increased by 25% to \$1,748,631, from \$1,402,900 for Fiscal 2001. This increase is a result of an increase in the cost of materials related to the development and formulation of new products not yet approved by the FDA.

Selling, general and administrative expenses in Fiscal 2002 increased by 61% to \$3,298,564, from \$2,014,004 for Fiscal 2001. This increase is a result of an increase in commissions to sales representatives for incremental sales programs, increased payroll and benefits expenses due to the hiring of additional administrative employees, and a general increase in other administrative expenses due to the growth of the Company, in terms of employees, production volume and sales.

As a result of the foregoing, the Company increased its operating income from \$2,139,325 for Fiscal 2001 to \$11,626,342 for Fiscal 2002.

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Included in other income for Fiscal 2001 is \$1,478,277 in income from the settlement of a lawsuit, net of fees. The lawsuit was initiated after a chemical supplier failed to supply the Company with raw material for its manufacturing process, despite the existence of a signed five-year supply contract. The Company alleged that the breach of contract delayed the introduction of one of its products into the marketplace. Consequently, the Company and the defending party settled the suit out of court. The Company received the proceeds in First Quarter Fiscal 2001. The Company incurred approximately \$305,000 in legal fees relating to the lawsuit. These fees were expensed to operations in Fiscal 2000.

The Company's interest expense decreased from \$778,008 for Fiscal 2001 to \$270,493 for Fiscal 2002 as a result of principal repayments and reduced interest rates. See Liquidity and Capital Resources below.

The Company's income tax expense increased from \$1,007,522 for Fiscal 2001 to \$3,984,135 for Fiscal 2002 as a result of the increase in taxable income.

The Company reported net income of \$7,195,990 for Fiscal 2002, or \$0.54 basic and diluted income per share, compared to net income of \$1,829,915 for Fiscal 2001, or \$0.14 basic and diluted income per share.

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### LIQUIDITY AND CAPITAL RESOURCES

Net cash provided by operating activities of \$7,436,861 for Fiscal 2002 was attributable to net income of \$7,195,990, as adjusted for the effects of non-cash items of \$1,713,402 and changes in operating assets and liabilities totaling (\$1,472,531). Significant changes in operating assets and liabilities are comprised of: (i) an increase in inventories of \$1,781,098 due primarily to the increases in raw materials and finished goods as a result of higher sales volume and the related inventory production, and larger buy-in's of certain raw materials, (ii) a decrease in accounts payable, net of the increase in accrued expenses, of \$95,441 due to increased operational expenses and capital equipment purchases and (iii) an increase in income taxes payable of \$478,443 due to higher taxable income and the accrual of the related income taxes, which will be paid when the Company's estimated tax filings and income tax returns are due.

The net cash used in investing activities of \$2,086,200 for Fiscal 2002 was attributable to \$1,952,535 expended for equipment and building additions, \$187,665 in deposits paid for equipment not yet received, and (\$54,000) in cash proceeds from the sale of equipment. The Company's anticipated budget for capital expenditures in Fiscal 2003 is approximately \$1,600,000. The anticipated additional capital expenditure requirements will support the Company's growth related to new product introductions and increased production output due to expected higher sales levels. As of June 30, 2002, none of the financing proceeds received from the bonds issued during Fiscal 1999 were available for future capital expenditures; however approximately \$188,000 was paid by the Company prior to June 30, 2002 for production equipment expected to arrive, and be placed in service in the Company's six months ended December 31, 2002. This balance is included in Other Assets at June 30, 2002.

The Company has a \$4,250,000 revolving line of credit from a shareholder who is also the Chairman of the Board ("Shareholder Line of Credit"). At June 30, 2002, the Company has no amount outstanding and \$4,250,000 available under this line of credit. The maturity date on the Shareholder Line of Credit was extended to December 1, 2002. There was no accrued interest at June 30, 2002 and June 30, 2001.

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In April 1999, the Company entered into a loan agreement (the "Agreement") with a governmental authority (the "Authority") to finance future construction and growth projects of the Company. The Authority has issued \$3,700,000 in tax-exempt variable rate demand and fixed rate revenue bonds to provide the funds to finance such growth projects pursuant to a trust indenture ("the "Trust indenture"). A portion of the Company's proceeds from the bonds was used to pay for bond issuance costs of approximately \$170,000. The remainder of the proceeds was deposited into a money market account, which is restricted to future plant and equipment needs of the Company as specified in the Agreement. The Trust Indenture requires the Company to repay the Authority loan through installment payments beginning in May 2003 and continuing through May 2014, the year the bonds mature. At June 30, 2002, the Company has \$3,700,000 outstanding on the Authority loan, of which \$356,667 is classified as currently due. The remainder is classified as a long-term liability. In April 1999, an irrevocable letter of credit of \$3,770,000 was issued by a bank to secure payment of the Authority Loan and a portion of the related accrued interest. At June 30, 2002, no portion of the letter of credit has been utilized.

In April 1999, the Company authorized and directed the issuance of \$2,300,000 in taxable variable rate demand and fixed rate revenue bonds pursuant to a trust indenture between the

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Company and a bank as trustee (the "Trust Indenture"). From the proceeds of the bonds, \$750,000 was utilized to pay deferred interest owed to Mr. Farber, the Chairman of the Board of Directors and Chief Executive Officer of the Company, and approximately \$1,440,000 was paid to a bank to refinance a mortgage term loan and equipment term loans. The remainder of the proceeds was used to pay bond issuance costs of approximately \$109,000. The Trust Indenture requires the Company to repay the bonds through installment payments beginning in June 1999 and continuing through May 2003, the year the bonds mature. At June 30, 2002, the Company has \$239,850 outstanding on the bonds, which is classified as currently due. In April 1999, an irrevocable letter of credit of approximately \$1,690,000 was issued by a bank to secure payment of the bonds and a portion of the related accrued interest. At June 30, 2002, no portion of the letter of credit has been utilized.

The Company has a \$2,000,000 line of credit from a bank. The line of credit was renewed and extended to November 30, 2002, at which time the Company expects to renew and extend the due date. The line of credit is limited to 80% of qualified accounts receivable and 50% of qualified inventory. At June 30, 2002, the Company had \$202,668 outstanding and \$1,797,332 available under the line of credit.

The Company believes that cash generated from its operations and the balances available under the Company's existing loans and lines of credit as of June 30, 2002, are sufficient to finance its level operations and currently anticipated capital expenditures.

Except as set forth in this report, the Company is not aware of any trends, events or uncertainties that have or are reasonably likely to have a material adverse impact on the Company's short-term or long-term liquidity or financial condition.

PROSPECTS FOR THE FUTURE

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As described above, additional products are also currently under development. Five of these products have been redeveloped and submitted to the Food and Drug Administration ("FDA") for supplemental approval. The remainder of the products in development represent either previously approved Abbreviated New Drug Applications ("ANDA's") which the Company is planning to reintroduce, or new formulations which the Company will submit ANDA's for FDA approval. The Company has also begun solicitation of quotes from outside contract development companies to supplement the Company's internal research and development efforts. Since the Company has no control over the FDA review process, management is unable to anticipate whether or when it will be able to begin producing and shipping additional products.

ITEM 7. FINANCIAL STATEMENTS

The Consolidated Financial Statements for the years ended June 30, 2002 and 2001 and Independent Auditor Report filed as a part of this Form 10-KSB are listed in the "Index to Financial Statements" filed herewith.

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ITEM 8. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

None

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PART III

ITEM 9. DIRECTORS, EXECUTIVE OFFICERS, PROMOTERS AND CONTROL PERSONS; COMPLIANCE WITH SECTION 16(A) OF THE EXCHANGE ACT

DIRECTORS AND EXECUTIVE OFFICERS

The directors and executive officers of the Company are set forth below:

	Age	Position
Directors:		
William Farber	71	Chairman of the Board
Marvin Novick	71	Director
Ronald A. West	68	Director

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Executive Officers:

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Arthur P. Bedrosian	55	President
Larry Dalesandro	30	Chief Operating Officer
Eugene Livshits	50	Vice President - Technical Affairs

WILLIAM FARBER was elected as Chairman of the Board of Directors in August 1991. From April 1993 to the end of 1993, Mr. Farber was the President and a director of Auburn Pharmaceutical Company. From 1990 through March 1993, Mr. Farber served as Director of Purchasing for Major Pharmaceutical Corporation. From 1965 through 1990, Mr. Farber was the Chief Executive Officer of Michigan Pharmacal Corporation. Mr. Farber is a registered pharmacist in the State of Michigan.

MARVIN NOVICK was elected a Director of the Company in February 2000. Mr. Novick has been an advisor, consultant and financial planner for multiple companies in the past thirty-five years. He is currently President of R&M Resources, Inc., an investment company. Previously, he has held the positions of Vice Chairman of Dura Corporation, a major automotive supplier, Partner of international accounting firm J.K. Lasser & Co., and Touche Ross & Co., Chief Financial Officer and Director of Meadowbrook Insurance Group, and Senior Vice President of Michigan Blue Shield, a major healthcare organization. Mr. Novick holds Bachelor's and Master's Degrees, and is a member of the American Institute of Certified Public Accountants.

RONALD A. WEST was elected a Director of the Company in January 2002. Mr. West is currently a Director of Beecher Associates, an industrial real estate investment company, R&M Resources, an investment and consulting services company and North East Staffing, Inc., an

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employee services company. Mr. West previously served as Chairman and Chief Executive Officer of Dura Corporation, an original equipment manufacturer of automotive products, including convertible tops, electrical and manual window regulators, truck utility step bumpers and other engineered equipment components. Prior to his service at Dura Corporation, Mr. West served in various financial management positions with TRW, Inc., Marlin Rockwell Corporation and National Machine Products Group. Mr. West studied Business Administration at Michigan State University and the University of Detroit.

ARTHUR P. BEDROSIAN, J.D. was elected President of the Company in May 2002. Prior to this, he served as the Company's Vice President of Business Development from January 2002 to April 2002, and as a Director from February 2000 to January 2002. Mr. Bedrosian has operated generic drug manufacturing, sales, and marketing businesses in the healthcare industry for many years. Prior to joining the Company, Mr. Bedrosian served as President and Chief Executive Officer of Trinity Laboratories, Inc., a medical device and drug manufacturer. Mr. Bedrosian also operated Pharmaceutical Ventures Ltd, a healthcare consultancy and Interall Corporation, a computer consultancy to Fortune 100 companies. Mr. Bedrosian holds a Bachelor of Arts Degree in Political Science from Queens College of the City University of New York and a Juris Doctorate from Newport University in California.

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LARRY DALESANDRO was elected Chief Operating Officer of the Company in November 1999. Mr. Dalesandro joined the Company in January 1999 to manage the Company's financial operations. Previously, he was the Chief Financial Officer of Criterion Communications, Inc., a technology and new media services firm, Controller of Crown Contractors, Inc., a contract construction company, and Senior Auditor of Grant Thornton LLP, an international professional services firm. Mr. Dalesandro graduated Magna Cum Laude with a Bachelor's of Science Degree in Accountancy from Villanova University, and is a Certified Public Accountant.

EUGENE LIVSHITS was elected Vice President Technical Affairs in November 1999. Dr. Livshits joined the Company in February 1997 as Director of Analytical Services. Dr Livshits has 27 years of experience in Analytical Services and Technical Affairs in the pharmaceutical industry. Dr. Livshits has previously been employed at Mutual Pharmaceutical Inc., PharmaKinetics Labs, Pal-Pak Inc., and Glenwood-Palisades Inc., where he held management and Director positions in Analytical Services. Dr. Livshits holds a Ph.D. from Moscow University.

To the best of the Company's knowledge, there have been no events under any bankruptcy act, no criminal proceedings and no judgments or injunctions that are material to the evaluation of the ability or integrity of any director or executive officer during the past five years.

ITEM 10. EXECUTIVE COMPENSATION

SUMMARY COMPENSATION TABLE

The following table summarizes all compensation paid to or earned by the executive officers of the Company for Fiscal 2002, Fiscal 2001 and Fiscal 2000. There are no other executive officers whose total salary and bonus for services rendered to the Company or any subsidiary exceeded \$100,000 during Fiscal 2002.

(A) Name and Principal Position -----	Annual Compensation				(E) Other Annual Compensation -----	(F) Restricted Stock Award(s) -----	Long Term
	(B) Fiscal Year ----	(C) Salary -----	(D) Bonus -----				Awards
William Farber	2002	0	0	0	0	0	
Chairman of the Board of Directors and Chief Executive Officer	2001	0	0	0	0	0	
	2000	0	0	0	0	0	
Arthur P. Bedrosian(3)	2002	64,385	0	3,000(1)	0	0	

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President	2001	0	0	0	0
	2000	0	0	0	0
Larry Dalesandro(3)	2002	116,698(2)	25,000	7,200(1)	0
Chief Operating Officer	2001	102,049(2)	5,000	3,600(1)	0
	2000	78,951(2)	5,000	3,600(1)	0
Eugene Livshits(3)	2002	126,715(2)	25,000	7,200(1)	0
Vice President/Technical Affairs	2001	109,669(2)	5,000	3,600(1)	0
	2000	96,043(2)	2,000	2,631(1)	0

- (1) Represents auto allowance.
- (2) Includes payments to the Company's 401(k) Plan (3% of eligible compensation).
- (3) Mr. Bedrosian was elected as an officer of the Company on January 24, 2002. Mr. Dalesandro and Mr. Livshits were elected as officers of the Company on November 1, 1999.

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- (4) The options represent 10,000 and 12,000 incentive stock options, which were granted to Mr. Dalesandro and Mr. Livshits, respectively on November 1, 2000 pursuant to the Company's 1993 Long Term Incentive Stock Plan. The options are exercisable as follows: one-third on or after November 1, 2000, one-third on or after November 1, 2001 and one-third on or after November 1, 2002.

OPTION EXERCISES AND YEAR END OPTION VALUES

(a)	(b)	(c)	(d)
NAME	SHARES ACQUIRED ON EXERCISE	VALUE REALIZED	NUMBER OF SECURITIES UNDERLYING UNEXERCISED OPTIONS AT FY-END EXERCISABLE/ UNEXERCISABLE
Larry Dalesandro Chief Operating Officer	6,666	\$69,993	0(1)/ 3,334(1)



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Eugene Livshits			0 (1) /
Vice President - of	8,000	\$68,800	4,000 (1)
Technical Affairs			

(1) The options represents an aggregate of 10,000 and 12,000 incentive stock options which were granted to Mr. Dalesandro and Mr. Livshits, respectively on November 1, 2000 pursuant to the Company's 1993 Long Term Incentive Stock Plan. The options are exercisable as follows: one-third on or after November 1, 2000, one-third on or after November 1, 2001 and one-third on or after November 1, 2002.

COMPENSATION OF DIRECTORS.

Directors received compensation of \$1,000 per meeting attended, for services provided as directors of the Company during Fiscal 2002. Directors are reimbursed for expenses incurred in attending Board meetings.

EMPLOYMENT CONTRACTS.

There were no employment contracts in existence at the end of Fiscal 2002.

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ITEM 11. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT

The following table sets forth, as of August 10, 2002, information regarding the security ownership of the directors and certain executive officers of the Company and persons known to the Company to be beneficial owners of more than five (5%) percent of the Company's common stock:

Name and Address of Beneficial Owner	Office	Excluding Options and Debentures	
		Number of Shares	Percent of Class
Directors/Executive Officers:			
Arthur Bedrosian 9000 State Road Philadelphia, PA 19136	President	302,750 (1)	1.81%
Larry Dalesandro 9000 State Road	Chief Operating Officer	6,666	0.05%

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Philadelphia, PA 19136

William Farber 9000 State Road Philadelphia, PA 19136	Chairman of the Board	9,134,486 (2)	68.87%
Eugene Livshits 9000 State Road Philadelphia, PA 19136	Vice President Technical Affairs	8,000	0.06%
Marvin Novick 9000 State Road Philadelphia, PA 19136	Director	52,200	.43%
Ronald A. West 9000 State Road Philadelphia, PA 19136	Director	150	0.00%
All directors and executive officers as a group (6 persons)		9,504,252	71.22%

(1) Includes 34,750 shares owned jointly by Arthur Bedrosian and Shari Bedrosian, Arthur Bedrosian's spouse, and 8,000 shares owned by Talin Bedrosian, Arthur Bedrosian's daughter.

(2) Includes 300,000 shares owned jointly by William Farber and Audrey Farber, the Secretary of the Company and William's Farber's spouse.

(3) Includes 30,000 vested options to purchase common stock at an exercise price of \$1.38 per share.

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\* Assumes that all options and debentures exercisable within sixty days have been exercised, which results in 13,358,737 shares outstanding.

### ITEM 12. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS

As described above, William Farber, the majority shareholder and Chairman of the Board of the Company, had provided the Company with a revolving line of credit due December 1, 2002 of \$4,250,000, which the Company has used to renovate its manufacturing facility, to acquire new equipment, to retain new management and to provide working capital. See MANAGEMENT'S DISCUSSION AND ANALYSIS -- Liquidity and Capital Resources." Mr. Farber is currently the holder of 9,134,486 shares of common stock of the Company, or approximately 69% of the Company's issued and outstanding shares. See "SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT."

The Company had sales of approximately \$174,000 and \$111,000 during the years ended June 30, 2002 and 2001, respectively, to a distributor (the "related party") in which the owner is the son of William Farber, the Chairman of the Board of Directors and principal shareholder of the Company. The Company also incurred sales commissions payable to the related party of approximately \$221,000 and \$369,000 during the years ended June 30, 2002 and 2001, respectively. Accounts receivable includes amounts due from the related party of approximately \$59,000 and \$34,000 at June 30, 2002 and June 30, 2001,

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respectively. Accrued expenses include amounts due to the related party of approximately \$8,000 and \$29,000 at June 30, 2002 and June 30, 2001, respectively. In the Company's opinion, the terms of these transactions were not more favorable than would have been from a non-related party.

ITEM 13. EXHIBITS AND REPORTS ON FORM 8-K

- (a) A list of the exhibits required by Item 601 of Regulation S-B to be filed as a part of this Form 10-KSB is shown on the Exhibit Index filed herewith.
- (b) The Company filed two reports on Form 8-K during the Quarter ended June 30, 2002. On April 16, 2002 the Company filed Form 8-K to disclose the fact that as of April 15th, 2002, the Company's common stock began trading on the American Stock Exchange. On May 10, 2002 the Company filed Form 8-K to disclose the fact that the Board of Directors elected Arthur Bedrosian as President of the Company.

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SIGNATURES

In accordance with Section 13 or 15(d) of the Exchange Act, the registrant caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

LANNETT COMPANY, INC.

Date: September 14, 2002  
-----

By: /s/ William Farber  
-----

William Farber,  
Chairman of the Board and  
Chief Executive Officer

Date: September 14, 2002  
-----

By: /s/ Larry Dalesandro  
-----

Larry Dalesandro,  
Chief Operating Officer

In accordance with the Exchange Act, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

Signature  
-----

Date  
-----

/ s / William Farber  
-----

September 14, 2002

William Farber,  
Chairman of the Board of Directors and  
Chief Executive Officer

I, William Farber and I, Larry Dalesandro, certify that:

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1. I have reviewed this report on Form 10-KSB of the Company;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial information included in this report, and the financial statements on which the financial information is based, fairly present in all material respects the financial condition, results of operations, changes in shareholders' equity, and cash flows the Company, as of, and for, the periods presented in this report;

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4. The Company's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the Company and we have:

a) designed such disclosure controls and procedures to ensure that material information relating to the Company, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

b) evaluated the effectiveness of the Company's disclosure controls and procedures as of a date within 90 days prior to the filing date of this report (the "Evaluation Date"); and

c) presented in this report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;

5. The Company's other certifying officers and I have disclosed, based on our most recent evaluation, to the Company's auditors and the audit committee of the Company's board of directors;

a) all significant deficiencies in the design or operation of internal controls which could adversely affect the Company's ability to record, process, summarize and report financial data and have identified for the Company's auditors any material weaknesses in internal controls; and

b) any fraud, whether or not material, that involves management or other employees who have a significant role in the Company's internal controls; and

6. The Company's other certifying officers and I have indicated in this report whether or not there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

Date: September 25, 2002

/s/ William Farber

-----  
Chairman of the Board of Directors and Chief Executive Officer

/s/ Larry Dalesandro

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Chief Operating Officer

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## Report of Independent Certified Public Accountants

Shareholders and Board of Directors  
Lannett Company, Inc. and Subsidiary

We have audited the accompanying consolidated balance sheets of Lannett Company, Inc. and Subsidiary as of June 30, 2002 and 2001, and the related consolidated statements of operations, changes in shareholders' equity and cash flows for each of the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Lannett Company, Inc. and Subsidiary as of June 30, 2002 and 2001, and the consolidated results of their operations and cash flows for each of the years then ended in conformity with accounting principles generally accepted in the United States of America.

Grant Thornton LLP  
Philadelphia, Pennsylvania  
August 14, 2002

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## CONSOLIDATED BALANCE SHEETS JUNE 30, 2002 AND 2001

ASSETS	2002
CURRENT ASSETS:	
Cash	\$ --
Trade accounts receivable (net of allowance of \$42,000 and \$25,000)	4,465,885
Inventories	4,937,207
Prepaid expenses and other assets	106,170
Deferred tax asset	300,368
Total current assets	9,809,630

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PROPERTY, PLANT AND EQUIPMENT	10,144,968
Less accumulated depreciation	3,616,044
	-----
	6,528,924
RESTRICTED CASH	--
OTHER ASSETS	369,949
DEFERRED TAX ASSET	--
	-----
TOTAL ASSETS	\$16,708,503
	=====
LIABILITIES AND SHAREHOLDERS' EQUITY	
CURRENT LIABILITIES:	
Line of credit	\$ 202,688
Line of credit-shareholder	--
Current portion of long-term debt	596,517
Accounts payable	733,984
Accrued expenses	657,891
Income taxes payable	726,552
	-----
Total current liabilities	2,917,632
LONG-TERM DEBT, LESS CURRENT PORTION	3,343,333
DEFERRED TAX LIABILITY	681,489
COMMITMENTS AND CONTINGENCIES	
SHAREHOLDERS' EQUITY:	
Common stock - authorized 50,000,000 shares, par value \$0.001;	
issued and outstanding, 13,263,838 and 13,206,128 shares, respectively	13,263
Additional paid-in capital	2,366,892
Retained earnings	7,385,894
	-----
Total shareholders' equity	9,766,049
	-----
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	\$16,708,503
	=====

See notes to consolidated financial statements.

CONSOLIDATED STATEMENTS OF OPERATIONS  
YEARS ENDED JUNE 30, 2002 AND 2001

-----  
2002

2001  
(RESTATED)

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NET SALES	\$ 25,126,214	\$ 12,090,993
COST OF SALES	8,452,677	6,534,764
	-----	-----
Gross profit	16,673,537	5,556,229
RESEARCH AND DEVELOPMENT EXPENSES	1,748,631	1,402,900
SELLING, GENERAL AND ADMINISTRATIVE EXPENSES	3,298,564	2,014,004
	-----	-----
Operating profit	11,626,342	2,139,325
	-----	-----
OTHER INCOME/(EXPENSE):		
Income from settlement of lawsuit, net of fees	--	1,475,814
Loss on sale of assets	(63,682)	(18,902)
Loss on abandonment of assets	(137,177)	(77,838)
Interest income	25,135	97,046
Interest expense, including \$131,245 and \$411,850 to shareholder	(270,493)	(778,008)
	-----	-----
	446,217	698,112
	-----	-----
INCOME BEFORE INCOME TAX EXPENSE	11,180,125	2,837,437
INCOME TAX EXPENSE	3,984,135	1,007,522
	-----	-----
NET INCOME	\$ 7,195,990	\$ 1,829,915
	=====	=====
Basic earnings per common share	\$ 0.54	\$ 0.14
	=====	=====
Diluted earnings per common share	\$ 0.54	\$ 0.14
	=====	=====

See notes to consolidated financial statements.

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CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY/(DEFICIENCY)  
YEARS ENDED JUNE 30, 2002 AND 2001

---

COMMON STOCK		ADDITIONAL PAID-IN CAPITAL	RETAINED EARNING (ACCUMULATED DEFICIT)
SHARES ISSUED	AMOUNT		

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BALANCE, JULY 1, 2000 (RESTATED)	\$13,206,128	13,206	\$ 2,312,575	\$ (1,640,011)
Net income (Restated)				1,829,915
BALANCE, JUNE 30, 2001	13,206,128	13,206	2,312,575	189,904
Exercise of stock options	57,710	57	54,317	--
Net income				7,195,990
BALANCE, JUNE 30, 2002	<u>13,263,838</u>	<u>\$ 13,263</u>	<u>\$ 2,366,892</u>	<u>\$ 7,385,894</u>

See notes to consolidated financial statements.

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CONSOLIDATED STATEMENTS OF CASH FLOWS  
YEARS ENDED JUNE 30, 2002 AND 2001

	2002	2001 (RESTATED)
OPERATING ACTIVITIES:		
Net income	\$ 7,195,990	\$ 1,829,915
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	789,304	767,047
Loss/Impairment on disposal of assets	200,859	96,740
Deferred tax expense/(benefit)	723,239	730,618
Changes in assets and liabilities which provided (used) cash:		
Trade accounts receivable	(99,298)	(3,269,069)
Inventories	(1,781,098)	(205,933)
Prepaid expenses and other assets	24,863	59,799
Accounts payable	(183,413)	170,197
Accrued expenses	87,972	25,420
Income taxes payable	478,443	248,109
	<u>7,436,861</u>	<u>452,843</u>
Net cash provided by operating activities		
INVESTING ACTIVITIES:		
Purchases of property, plant and equipment	(1,952,535)	(1,488,741)
Deposits paid on machinery and equipment not yet received	(187,665)	--
Proceeds from sale of property, plant and equipment	54,000	43,250
	<u>(2,086,200)</u>	<u>(1,445,491)</u>
Net cash used in investing activities		



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FINANCING ACTIVITIES:

Net borrowings/(repayments) under line of credit	(1,797,312)	941,476
Repayments under line of credit - shareholder	(4,225,000)	
Repayments of debt	(608,372)	(749,624)
Proceeds from debt, net of restricted cash released	1,225,649	800,796
Proceeds from issuance of stock	54,374	--
	-----	-----
Net cash provided by/(used in) financing activities	(5,350,661)	992,648
	-----	-----
NET INCREASE (DECREASE) IN CASH	--	--
CASH, BEGINNING OF YEAR	--	--
	-----	-----
CASH, END OF YEAR	\$ --	\$ --
	=====	=====
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION -		
Interest paid during year	\$ 293,323	\$ 800,171
	=====	=====
Income taxes paid	\$ 2,782,453	\$ 54,682
	=====	=====

See notes to consolidated financial statements.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
YEARS ENDED JUNE 30, 2002 AND 2001

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Lannett Company, Inc. and subsidiaries (the "Company"), a Delaware corporation, develops, manufactures, packages, markets and distributes pharmaceutical products sold under generic chemical names. In addition, the Company contract manufactures and private labels pharmaceutical products for other companies. Currently, the Company manufactures only solid oral dosage forms, including tablets and capsules; but the Company is pursuing partnerships and research contracts for the development and production of other dosage forms, including liquids and injectable products.

The Company is engaged in an industry which is subject to considerable government regulation related to the development, manufacturing and marketing of pharmaceutical products. In the normal course of business, the Company periodically responds to inquiries or engages in administrative and judicial proceedings involving regulatory authorities, particularly the Food and Drug Administration (FDA) and the Drug Enforcement Agency (DEA).

RESTATEMENT - The Company has corrected and restated its Fiscal 2001 financial statements due to the correction of an error resulting from the improper deferral of legal fees at June 30, 2000 incurred associated with the favorable settlement of a lawsuit. The effect of the restatement for the year ended June 30, 2001 was to increase other income and previously reported net income by

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\$305,128, or \$.02 per diluted share. This impact is reflected in the reported results herein. There was no effect of the restatement as of June 30, 2001 in total assets, total liabilities, or retained earnings.

**PRINCIPLES OF CONSOLIDATION** - The consolidated financial statements include the accounts of Lannett Company, Inc., its inactive wholly owned subsidiary, Astrochem Corporation and its wholly owned subsidiary, Lannett Holdings, Inc. All intercompany accounts and transactions have been eliminated.

**REVENUE RECOGNITION** - The Company recognizes revenue when its products are shipped. Under a contract in which product development occurs, the Company recognizes revenue when services are rendered. There are no inventory consignments held at customers' locations. Provisions for estimated rebates, chargebacks, returns and other adjustments are provided for in the period the related sales are recorded. If the historical data the Company uses to calculate these estimates does not accurately approximate future activity, its net sales, gross profit, net income and earnings per share could decrease. However, management believes that these estimates are reasonable based upon historical experience and current conditions.

**INVENTORIES** - Inventories are valued at the lower of cost (determined under the first-in, first-out method) or market.

**PROPERTY, PLANT AND EQUIPMENT** - Property, plant and equipment are stated at cost. Depreciation and amortization are provided for by the straight-line and accelerated methods over estimated useful lives of the assets. Depreciation expense for the years ended June 30, 2002 and 2001 was approximately \$789,000 and \$725,000, respectively.

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**DEFERRED DEBT ACQUISITION COSTS** - Costs incurred in connection with obtaining financing are amortized by the straight-line method over the term of the loan arrangements. Amortization expense for the years ended June 30, 2002 and 2001 was approximately \$42,000.

**RESEARCH AND DEVELOPMENT** - Research and development expenses are charged to operations as incurred.

**ADVERTISING COSTS** - The Company charges advertising costs to operations as incurred. Advertising expense for the years ended June 30, 2002 and 2001 was approximately \$16,000 and \$4,000, respectively.

**INCOME TAXES** - The Company uses the liability method specified by Statement of Financial Accounting Standards (SFAS) No. 109, Accounting for Income Taxes. Deferred tax assets and liabilities are determined based on the difference between the financial statement and tax bases of assets and liabilities as measured by the enacted tax rates which will be in effect when these differences reverse. Deferred tax expense (benefit) is the result of changes in deferred tax assets and liabilities.

**LONG-LIVED ASSETS** - SFAS No. 121, Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of, provides guidance on when to recognize and how to measure impairment losses of long-lived assets and certain identifiable intangibles and how to value long-lived assets to be disposed of. Impairment losses recognized during the years ended June 30, 2002 and 2001 were \$225,256 and \$77,838, respectively (See NEW ACCOUNTING PRONOUNCEMENTS).

**EARNINGS PER COMMON SHARE** - SFAS No. 128, Earnings Per Share, requires a dual

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presentation of basic and diluted earnings per share on the face of the Company's consolidated statement of income and a reconciliation of the computation of basic earnings per share to diluted earnings per share. Basic earnings per share excludes the dilutive impact of common stock equivalents and is computed by dividing net income by the weighted-average number of shares of common stock outstanding for the period. Diluted earnings per share includes the effect of potential dilution from the exercise of outstanding common stock equivalents into common stock using the treasury stock method. Earnings per share amounts for all periods presented have been calculated in accordance with the requirements of SFAS No. 128. A reconciliation of the Company's basic and diluted earnings per share follows:

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	2002		2001	
	NET INCOME (NUMERATOR)	SHARES (DENOMINATOR)	NET INCOME (NUMERATOR)	SHA (DENOM
Basic earnings per share factors	\$7,195,990	13,263,838	\$1,829,915	13,20
Effect of potentially dilutive option plans and debentures		81,861		
	\$7,195,990	13,345,699	\$1,829,915	13,20
	=====	=====	=====	=====
Basic earnings per share	\$ 0.54		\$ 0.14	
Diluted earnings per share	\$ 0.54		\$ 0.14	

Options to purchase 44,355 shares, 15,835 shares, 10,000 shares, 30,000 shares and 1,050 shares of common stock at \$1.125 per share, \$0.80 per share, \$3.45 per share, \$1.38 per share and \$3.78 per share, respectively, were outstanding at June 30, 2002. Options to purchase 68,450 shares, 51,500 shares, 30,000 shares and 1,300 shares of common stock at \$1.125 per share, \$0.80 per share, \$1.38 per share and \$3.78 per share, respectively, were outstanding at June 30, 2001, but were not included in the computation of diluted earnings per share because to do so would be antidilutive.

STOCK OPTION PLAN - SFAS No. 123, Accounting for Stock-Based Compensation, encourages, but does not require companies to record compensation cost for stock-based employee compensation plans at fair value. The Company has chosen to continue to account for stock-based compensation in accordance with Accounting Principles Board Opinion (APB) No. 25, Accounting for Stock Issued to Employees, under which no compensation cost has been recognized (See Note 10).

SEGMENT INFORMATION - The Company reports segment information in accordance with SFAS No. 131, Disclosures about Segments of an Enterprise and Related Information. The Company operates one business segment--generic pharmaceuticals. In accordance with SFAS No. 131, the Company aggregates all products and reports one operating segment. Within this segment, the Company manufactures and sells a line of both prescription (Rx) and over-the-counter (OTC) drug products. All of

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these products are either tablets or capsules sold generically to the drug distribution industry. The only difference in the product line is the status that the Food and Drug Administration gives the product--either prescription status in which a doctor prescribes or authorizes the consumer to obtain the product, or over-the-counter status, which allows consumers to purchase the product directly from retailers without a doctor's prescription. There are no operating differences for the Company in the manufacture of such lines of product that would require the Company to perform separate profitability analyses, or segregate income and loss activities by its status, as described above. Additionally, management does not prepare separate income and loss statements, forecasts and/or budget plans for its Rx versus OTC product lines. For its Fiscal years ended June 30, 2002 and 2001, Rx sales were \$21,806,156 and \$7,299,273 respectively. For its Fiscal years ended June 30, 2002 and 2001, OTC sales were \$3,320,058 and \$4,791,717 respectively.

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CONCENTRATION OF CREDIT RISK - Two customers accounted for approximately \$5,488,000 (22%) and \$4,886,000 (19%) of net sales, respectively, in the fiscal year ended June 30, 2002. One customer accounted for approximately \$2,905,000 (24%) of net sales in the fiscal year ended June 30, 2001. The Company performs ongoing credit evaluations of its customers' financial condition and has experienced no significant collection problems to date. Generally, the Company requires no collateral from its customers. One of the Company's products accounted for approximately \$13,461,000 (54%) of net sales in fiscal year ended June 30, 2002. Two of the Company's products accounted for approximately \$4,445,000 (37%) and \$4,167,000 (34%) of net sales in fiscal year ended June 30, 2001. The Company expects these percentages to decrease as it continues to market additional products.

USE OF ESTIMATES - The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America 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. Actual results could differ from those estimates.

### NEW ACCOUNTING PRONOUNCEMENTS

On July 20, 2001, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards (SFAS) 141, Business Combinations, and SFAS 142, Goodwill and Intangible Assets. SFAS 141 is effective for all business combinations completed after June 30, 2001. SFAS 142 is effective for fiscal years beginning after December 15, 2001; however, certain provisions of this Statement apply to goodwill and other intangible assets acquired between July 1, 2001 and the effective date of SFAS 142. Major provisions of these Statements and their effective dates for the Company are as follows:

- all business combinations initiated after June 30, 2001 must use the purchase method of accounting. The pooling of interest method of accounting is prohibited except for transactions initiated before July 1, 2001.
- intangible assets acquired in a business combination must be recorded separately from goodwill if they arise from contractual or other legal

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- rights or are separable from the acquired entity and can be sold, transferred, licensed, rented or exchanged, either individually or as part of a related contract, asset or liability
- goodwill, as well as intangible assets with indefinite lives, acquired after June 30, 2001, will not be amortized. Effective July 1, 2002, all previously recognized goodwill and intangible assets with indefinite lives will no longer be subject to amortization.
  - Effective July 1, 2002, goodwill and intangible assets with indefinite lives will be tested for impairment annually and whenever there is an impairment indicator
  - all acquired goodwill must be assigned to reporting units for purposes of impairment testing and segment reporting.

Although it is still reviewing the provisions of these Statements, management's preliminary assessment is that these Statements will not have a material impact on the Company's financial position or results of operations.

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In August 2001, the FASB issued SFAS 143, Accounting for Asset Retirement Obligations. SFAS 143 applies to all entities, including rate-regulated entities, that have legal obligations associated with the retirement of a tangible long-lived asset that result from acquisition, construction or development and (or) normal operations of the long-lived asset. The application of this Statement is not limited to certain specialized industries, such as the extractive or nuclear industries. This Statement also applies, for example, to a company that operates a manufacturing facility and has a legal obligation to dismantle the manufacturing plant and restore the underlying land when it ceases operation of that plant. A liability for an asset retirement obligation should be recognized if the obligation meets the definition of a liability and can be reasonably estimated. The initial recording should be at fair value. SFAS 143 is effective for financial statements issued for fiscal years beginning after June 15, 2002, with earlier application encouraged. The provisions of the Statement are not expected to have a material impact on the financial condition or results of operations of the Company.

In August 2001, the FASB issued SFAS 144, Accounting for the Impairment or Disposal of Long-Lived Assets. SFAS No. 144 retains the existing requirements to recognize and measure the impairment of long-lived assets to be held and used or to be disposed of by sale. However, SFAS 144 makes changes to the scope and certain measurement requirements of existing accounting guidance. SFAS 144 also changes the requirements relating to reporting the effects of a disposal or discontinuation of a segment of a business. SFAS 144 is effective for financial statements issued for fiscal years beginning after December 15, 2001 and interim periods within those fiscal years. The adoption of this statement is not expected to have a significant impact on the financial condition or results of operations of the Company.

In April 2002, FASB issued SFAS 145, Rescission of FASB Statements No. 4, 44 and 64, Amendment of FASB No. 13, and Technical Corrections. SFAS No. 145 changes the accounting principles governing extraordinary items by clarifying and, to some extent, modifying the existing definition and criteria, specifying disclosure for extraordinary items and specifying disclosure requirements for other unusual or infrequently occurring events and transactions that are not extraordinary items. SFAS 145 is effective for financial statements issued for fiscal years beginning after June 15, 2002, with early adoption encouraged. The adoption of this statement is not expected to have a significant impact on the financial condition or results of operations of the Company.

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RECLASSIFICATIONS - Certain reclassifications were made to the 2001 consolidated financial statements to conform to the 2002 presentation.

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### 2. INVENTORIES

Inventories at June 30, 2002 and 2001 consist of the following:

	2002	2001
Raw materials	\$2,479,344	\$1,516,030
Work-in-process	691,346	686,359
Finished goods	1,560,029	712,992
Packaging supplies	206,488	240,728
	-----	-----
	\$4,937,207	\$3,156,109
	=====	=====

### 3. PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment at June 30, 2002 and 2002 consist of the following:

	USEFUL LIVES	2002
Land	-	\$ 33,414
Building and improvements	10 - 39 years	3,124,268
Machinery and equipment	5 - 10 years	6,877,429
Furniture and fixtures	5 - 7 years	109,857
		-----
		\$10,144,968
		=====

### 4. CASH EQUIVALENTS

The Company considers all highly liquid debt instruments and other short-term investments with an initial maturity date of three months or less from purchase date to be cash equivalents.

### 5. BANK LINE OF CREDIT

The Company has a \$2,000,000 line of credit with a bank that bears interest at prime plus .50% per annum (5.25% at June 30, 2002). The line of credit is due November 30, 2002. The Company expects to extend the maturity date before the scheduled due date. The line of credit is limited to 80% of qualified accounts receivable and 50% of qualified inventory. At June 30, 2002, the Company had \$202,688 outstanding, and \$1,797,312 available under the line of credit. The line of credit is collateralized by substantially all Company assets and a personal guarantee of the major shareholder. Further, the line of credit and a

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related letter of credit contain certain financial covenants (see Note 6).

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### 6. LONG-TERM DEBT

Long-term debt at June 30, 2002 and 2001 consists of the following:

	2002	
Tax-exempt Bond Loan	\$3,700,000	\$3
Taxable Bond Loan	239,850	---
	-----	---
	3,939,850	4
Less current portion	596,517	---
	-----	---
	\$3,343,333	\$3
	=====	==

In April 1999, the Company entered into a loan agreement (the "Agreement") with a governmental authority (the "Authority") to finance future construction and growth projects of the Company. The Authority has issued \$3,700,000 in tax-exempt variable rate demand and fixed rate revenue bonds to provide the funds to finance such growth projects pursuant to a trust indenture (the "Trust Indenture"). The bonds were issued under and secured by a Trust Indenture between the Authority and a bank, as trustee. A portion of the Company's proceeds from the bonds was used to pay for bond issuance costs of approximately \$170,000. The remainder of the proceeds was deposited into a money market account which is restricted to future plant and equipment needs of the Company as specified in the Agreement (see Note 4). The Agreement requires the Company to repay the Authority loan through installment payments beginning in May 2003 and continuing through May 2014, the year the bonds mature. Such payments will be deposited into an interest-bearing debt service money market account. The bonds bear interest at the floating variable rate determined by the organization responsible for selling the bonds (the "remarketing agent"). The interest rate fluctuates on a weekly basis. The effective interest rate at June 30, 2002 was 2.85%. The Company has an option to convert the bonds to a fixed rate of interest under certain conditions. At June 30, 2002, the Company has \$3,700,000 outstanding on the Authority loan, of which \$356,667 is classified as currently due. The remainder is classified as a long-term liability. In April 1999, an irrevocable letter of credit of \$3,770,000 was issued by a bank to secure payment of the Authority loan and a portion of the related accrued interest. At June 30, 2002, no portion of the letter of credit has been utilized.

In April 1999, the Company authorized and directed the issuance of \$2,300,000 in taxable variable rate demand and fixed rate revenue bonds pursuant to a trust indenture between the Company and a bank, as trustee (the "Trust Indenture"). From the proceeds of the bonds, \$750,000 was utilized to pay deferred interest owed to the principal shareholder of the Company and approximately \$1,440,000 was paid to a bank to refinance a mortgage term loan and equipment term loans. The remainder of the proceeds was used to pay bond issuance costs of approximately \$109,000. The Trust Indenture requires the Company to repay the bonds through installment payments beginning in May 2000 and continuing through May 2003, the year the bonds mature. Such payments will be deposited into an

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interest-bearing debt service money market account. The bonds bear interest at the floating variable rate determined by the organization responsible for selling the bonds (the "remarketing agent"). The interest rate fluctuates on a weekly basis. The effective interest rate at June 30, 2002 was 4.06%. The Company has an option to convert the bonds to a fixed rate of interest under certain conditions. At June 30, 2002, the Company has \$239,850 outstanding on the bonds, which is classified as currently due. In April 1999, an irrevocable letter of credit of approximately \$1,690,000 was

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issued by a bank to secure payment of the bonds and a portion of the related accrued interest. At June 30, 2002, no portion of the letter of credit has been utilized.

Annual repayments of debt, including sinking fund requirements, as of June 30, 2002 are as follows:

YEAR ENDING JUNE 30,	AMOUNTS PAYABLE TO INSTITUTIONS
2003	\$ 596,517
2004	718,333
2005	706,667
2006	678,333
2007	300,000
Thereafter	940,000
	-----
	\$3,939,850
	=====

### 7. LINE OF CREDIT PAYABLE TO SHAREHOLDER

On October 1, 2001, a debt modification agreement was consummated, by and between, the Company and its principal shareholder relating to the line of credit agreement described below. The Company and its principal shareholder had previously modified the debt agreement relating to the line of credit as of March 15, 1993, August 1, 1994, May 15, 1995, December 31, 1995, June 30, 1996, November 1, 1996, September 9, 1997, June 30, 1998, December 30, 1998, December 31, 1999 and October 1, 2000. In each of the modifications, the maturity date of the debt was extended.

The Company has a \$4,250,000 revolving line of credit from a shareholder who is also the Chairman of the Board. At June 30, 2002, the Company had \$0 outstanding and \$4,250,000 available under this line of credit. The expiration date of the line is December 1, 2002.

The line of credit bears interest at the prime rate published by Michigan National Bank plus 1% per annum. The effective rate at June 30, 2002 was 5.75%. Interest expense during the years ended June 30, 2002 and 2001 was approximately \$132,245, and \$412,000, respectively. Accrued interest at June 30, 2002 and June 30, 2001 was \$0.



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The line of credit is collateralized by substantially all Company assets, and is subordinated to the bank letters of credit and line of credit.

### 8. INCOME TAXES

The provision (benefit) for income taxes consists of the following for the years ended June 30, 2002 and 2001.

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	2002	2001
Current	\$3,260,896	\$ 276,904
Deferred	723,239	730,618
	-----	-----
	\$3,984,135	\$1,007,522
	=====	=====

A reconciliation of the differences between the effective rates and statutory rates is as follows:

	2002	2001
Federal income tax at statutory rate	34.0 %	34.0 %
State and local income tax, net	3.1	6.8
Change in the beginning of the year balance of the valuation allowance		
Other	(1.5)	(1.0)
	----	----
Income taxes expense/(benefit)	35.6 %	39.8 %
	====	====

The principal types of differences between assets and liabilities for financial statement and tax return purposes are net operating loss carryforwards and accumulated depreciation. As of June 30, 2002, the Company has utilized all of its available federal net operating loss carryforwards of approximately \$2,457,000. A deferred tax liability is recorded for the future liability created by different depreciation methods for financial statement and tax return purposes.

Temporary differences which give rise to deferred tax assets and liabilities are as follows as of June 30, 2002 and 2002:

	2002
Deferred tax assets:	
Accrued expenses	\$ 38,370
Net operating loss carryforward	835,700
Other	261,998

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	-----
	300,368
Valuation allowance	--
	-----
Total	300,368
Deferred tax liability - Property, plant and equipment	681,489
	-----
Net deferred tax asset/(liability)	\$(381,121)
	=====

9. STOCK OPTIONS

In fiscal 1993, the Company adopted the 1993 Long-Term Incentive Plan (the "Plan"). Pursuant to the Plan, officers and key employees of the Company may be granted stock options which qualify as incentive stock options as well as stock options which are nonqualified. The exercise

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price of the options is at least the fair market value of the common stock on the date of grant. The options vest over a three-year period and expire no later than 10 years from the date of grant. There are 2,000,000 shares reserved under the Plan. Options for 1,822,915 shares remain unissued as of June 30, 2002.

The Company accounts for the Plan in accordance with APB Opinion No. 25, under which no compensation cost has been recognized. Had compensation cost for the Plan been determined consistent with SFAS No. 123, Accounting for Stock-Based Compensation, the Company's net income would have been reduced by \$90,302 and \$75,175 for the years ended June 30, 2002 and 2001, respectively, and earnings per share would have been reduced by \$0.01 per share for the years ended June 30, 2002 and 2001.

A summary of the status of the Company's option plan as of June 30, 2002 and 2001 and the changes during the years then ended is represented below:

	2002	
	-----	
	SHARES	WEIGHTED EXERCISE PRICE
Outstanding, beginning of year	151,250	\$ 1.
Granted	10,000	3.
Exercised	(56,676)	0.
Terminated	(3,334)	0.
	-----	
Outstanding, end of year	101,240	\$ 1.
	=====	
Options exercisable at year-end	95,933	\$ 1.
	=====	
Weighted average fair value of options granted during the year		\$ 3.

=====

The fair value of the options granted were estimated on the date of grant using the Black-Scholes option-pricing model with the following assumptions for grants during the years ended June 30, 2002 and 2001: risk-free interest rate of 5.15% and 5.42%, expected volatility of 70.6% and 57.5%, dividend yield of 0%, and expected life of 5 years.

RANGE OF EXERCISE PRICES	OPTIONS	WEIGHTED AVERAGE REMAINING CONTRACTUAL LIFE IN YEARS
\$0.80 - \$1.125	60,190	7.3
\$1.38	30,000	5.3
\$3.45	10,000	9.5
\$3.78	1,050	1.8

#### 10. EMPLOYEE BENEFIT PLAN

The Company has a defined contribution plan (the "Plan") covering substantially all employees. The Company is required to contribute amounts pursuant to employee salary reduction agreements and a matching contribution equal to each employee's contribution not to exceed 3%

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of the employee's compensation for the Plan year. Contributions to the Plan during the years ended June 30, 2002 and 2001 were \$86,222 and \$70,891, respectively.

#### 11. CONTINGENCIES

The Company monitors its compliance with all environmental laws. Any compliance costs which may be incurred are contingent upon the results of future site monitoring and will be charged to operations when incurred. No monitoring costs were incurred during the years ended June 30, 2002 and 2001.

The Company is currently engaged in several civil actions as a co-defendant with many other manufacturers of Diethylstilbestrol ("DES"), a synthetic hormone. Prior litigation established that the Company's pro rata share of any liability is less than one-tenth of one percent. The Company was represented in many of these actions by the insurance company with which the Company maintained coverage (subject to limits of liability) during the time period that damages were alleged to have occurred. The Company has either settled or is currently defending over 500 such claims. Management believes that the outcome will not have a material adverse impact on the consolidated financial position or results of operations of the Company.

In addition to the matters reported herein, the Company is involved in litigation which arises in the normal course of business. In the opinion of

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management, the resolution of these lawsuits will not have a material adverse effect on the consolidated financial position or results of operations.

### 12. COMMITMENTS

In January 1998, the Company entered into an operating lease for additional space. Currently, this leased facility houses the shipping and receiving department, warehousing, and the research and development laboratory. The lease was extended through April 30, 2004. The Company also has another operating lease, expiring in 2005, for office equipment. Future minimum lease payments under these agreements are as follows:

YEAR ENDING JUNE 30,	AMOUNT
2003	\$ 132,255
2004	112,380
2005	11,935
	-----
	\$ 256,570
	=====

Rental expense for the years ended June 30, 2002 and 2001 was \$124,000 and \$123,000, respectively.

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### 13. RELATED PARTY TRANSACTIONS

The Company had sales of approximately \$174,000 and \$111,000 during the years ended June 30, 2002 and 2001, respectively, to a distributor (the "related party") in which the owner is a relative of the Chairman of the Board of Directors and principal shareholder of the Company. The Company also incurred sales commissions payable to the related party of approximately \$221,000 and \$369,000 during the years ended June 30, 2002 and 2001, respectively. Accounts receivable includes amounts due from the related party of approximately \$59,000 and \$34,000 at June 30, 2002 and June 30, 2001, respectively. Accrued expenses include amounts due to the related party of approximately \$8,000 and \$29,000 at June 30, 2002 and June 30, 2001, respectively.

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### EXHIBIT INDEX

Exhibit Number -----	Description -----	Method of Filing -----
3(a)	Articles of Incorporation	Incorporated by reference to the Proxy Stat with respect to the Annual Meeting of Sha on December 6, 1991 (the "1991 Proxy Stat

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3(b)	By-Laws, as amended	Incorporated by reference to the 1991 Pro
4(a)	Specimen Certificate for Common Stock	Incorporated by reference to Exhibit 4(a) April 23, 1993 (Amendment No. 3 to Form 10-KSB f/y/e June 30, 1992) ("Form 8")
10(a)	Loan Agreement dated August 30, 1991 between the Company and William Farber	Incorporated by reference to the Annual Report on Form 10-K f/y/e June 30, 1991
10(b)	Amendment #1 to Loan Agreement dated March 15, 1993	Incorporated by reference to Exhibit 10(b) Report on Form 10-KSB f/y/e June 30, 1993 ("Form 10-K")
10(c)	Amendment #2 to Loan Agreement dated August 1, 1994	Incorporated by reference to Exhibit 10(c) Report on Form 10-KSB f/y/e June 30, 1994 ("Form 10-K")
10(d)	Amendment #3 to Loan Agreement dated May 15, 1995	Incorporated by reference to Exhibit 10(d) Report on Form 10-KSB f/y/e June 30, 1995 ("Form 10-K")
10(e)	Amendment #4 to Loan Agreement dated December 31, 1995	Incorporated by reference to Exhibit 10(e) Report on Form 10-KSB f/y/e June 30, 1996 ("Form 10-K")
10(f)	Amendment #5 to Loan Agreement dated June 30, 1996	Incorporated by reference to Exhibit 10(f) Report on Form 10-KSB f/y/e June 30, 1996 ("Form 10-K")

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Exhibit Number -----	Description -----	Method of Filing -----
10(g)	Amendment #6 to Loan Agreement dated November 1, 1996	Incorporated by reference to Exhibit 10(g) Report on Form 10-KSB f/y/e June 30, 1997 ("Form 10-KSB")
10(h)	Amendment #7 to Loan Agreement dated September 9, 1997	Incorporated by reference to Exhibit 10(h) Report on 1997 Form 10-KSB
10(i)	Amendment #8 to Loan Agreement dated June 30, 1998	Incorporated by reference to Exhibit 10(i) Report on 1998 Form 10-KSB
10(j)	Amendment #9 to Loan Agreement dated December 31, 1998	Incorporated by reference to Exhibit 10(j) Quarterly Report on for the period ended
10(k)	Amendment #10 to Loan Agreement dated December 31, 1998	Incorporated by reference to Exhibit 10(k) Report on Form 10-KSB for Fiscal Year 2000
10(l)	Loan Agreement dated May 4, 1993 between the Company and Meridian Bank	Incorporated by reference to Exhibit 10(c) Form 10-K
10(m)	Amendment to Loan Documents between the Company and Meridian Bank dated as of December 8, 1993	Incorporated by reference to Exhibit 10(e) Report on Form 10-KSB f/y/e June 30, 1994 ("Form 10-K")

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10(n)	Letter Agreement between the Company and Meridian Bank dated December 21, 1993	Incorporated by reference to Exhibit 10(f) Report on Form 10-KSB f/y/e June 30, 1994 10-K")
10(o)	Third Amendment to Loan Agreement dated as of June 9, 1994	Incorporated by reference to Exhibit 10(g) Report on Form 10-KSB f/y/e June 30, 1994 10-K")
10(p)	Fourth Amendment to Loan Documents between the Company and Meridian Bank as of October 27, 1994	Incorporated by reference to Exhibit 10(i) Report on Form 10-KSB f/y/e June 30, 1995 10-K")

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Exhibit Number -----	Description -----	Method of Filing -----
10(q)	Letter Agreement between the Company and Meridian Bank dated October 27, 1994	Incorporated by reference to Exhibit 10(j) Report on Form 10-KSB f/y/e June 30, 1995 10-K")
10(r)	Letter Agreement between the Company and Meridian Bank dated July 10, 1995	Incorporated by reference to Exhibit 10(k) Report on Form 10-KSB f/y/e June 30, 1995 10-K")
10(s)	Amendment to Security Agreement between the Company and Meridian Bank dated as of July 31, 1995	Incorporated by reference to Exhibit 10(l) Report on Form 10-KSB f/y/e June 30, 1995 10-K")
10(t)	Line of Credit Note dated July 31, 1995	Incorporated by reference to Exhibit 10(m) Report on Form 10-KSB f/y/e June 30, 1995 10-K")
10(u)	Fifth Amendment to Loan Agreement dated July 31, 1995	Incorporated by reference to Exhibit 10(n) Report on Form 10-KSB f/y/e June 30, 1995 10-K")
10(v)	Amendment to Loan agreement between the Company and Meridian Bank, dated March 5, 1996.	Incorporated by reference to Exhibit 10(q) Report on Form 10-KSB f/y/e June 30, 1996 10-K")
10(w)	Amendment to Loan agreement between the Company and Corestates Bank, dated March 20, 1997.	Incorporated by reference to Exhibit 10(h) Report on 1997 Form 10-KSB
10(x)	Amendment to Loan agreement between the Company and Corestates Bank, dated March 20, 1997.	Incorporated by reference to Exhibit 10(h) Report on 1997 Form 10-KSB

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Exhibit Number -----	Description -----	Method of Filing -----
10(y)	Amendment to Loan agreement between the Company and Corestates Bank, dated May 23, 1997.	Incorporated by reference to Exhibit 10(h) Report on 1997 Form 10-KSB
10(z)	Amendment to Loan agreement between the Company and Corestates Bank, dated September 24, 1997.	Incorporated by reference to Exhibit 10(h) Report on 1997 Form 10-KSB
10(aa)	Amendment to Loan agreement between the Company and Corestates Bank, dated December 10, 1997.	Incorporated by reference to Exhibit 10(h) Report on 1997 Form 10-KSB
10(ab)	Amendment to Loan agreement between the Company and Corestates Bank, dated December 10, 1997.	Incorporated by reference to Exhibit 10(h) Report on 1997 Form 10-KSB
10(ac)	Amendment to Loan agreement between the Company and Corestates Bank, dated June 11, 1998.	Incorporated by reference to Exhibit 10(a) Report on 1998 Form 10-KSB
10(ad)	Amendment to Loan agreement between the Company and Corestates Bank, dated on 1998 Form 10-KSB June 1998.	Incorporated by reference to Exhibit 10(a) Report
10(ae)	Line of Credit Note dated March 11, 1999	Incorporated by reference to Exhibit 10(a) Report on 1999 Form 10-KSB
10(af)	Taxable Variable Rate Demand/Fixed Rate Revenue Bonds, Series of 1999	Incorporated by reference to Exhibit 10(a) Report on 1999 Form 10-KSB
10(ag)	Philadelphia Authority for Industrial Development Tax-Exempt Variable Rate Demand/Fixed Revenue Bonds (Lannett Company, Inc. Project) Series of 1999	Incorporated by reference to Exhibit 10(a) Report on 1998 Form 10-KSB

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Exhibit Number -----	Description -----	Method of Filing -----
10(ah)	Letter of Credit and Agreements supporting bond issues	Incorporated by reference to Exhibit 10(a) Report on 1998 Form 10-KSB
10(ai)	Employment agreement between the Company and Vlad Mikijanic	Incorporated by reference to Exhibit 10(i) Report on Form 10-KSB f/y/e June 30, 1994 10-K")
10(aj)	Supply Agreement dated January 14, 1997	Incorporated by reference to Exhibit 10(a) Report on 1998 Form 10-KSB
10(ak)	Supply Agreement dated January 17, 1997	Incorporated by reference to Exhibit 10(a)

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		Report on 1998 Form 10-KSB
10(a)	Supply Agreement dated January 17, 1997	Incorporated by reference to Exhibit 10(a) Report on 1998 Form 10-KSB
10(am)	Supply Agreement dated February 11, 1997	Incorporated by reference to Exhibit 10(a) Report on 1998 Form 10-KSB
10(an)	Supply Agreement dated May 27, 1997	Incorporated by reference to Exhibit 10(a) Report on 1998 Form 10-KSB
11	Computation of Earnings Per Share	Filed Herewith
22	Subsidiaries of the Company	Incorporated by reference to the Annual R 10-K f/y/e June 30, 1990
23	Consent of Deloitte & Touche	Incorporated by reference to Exhibit 23 t Report on 1999 Form 10-KSB
24	Certification Pursuant to 18 USC Section 1350	Filed Herewith