CHROMATICS COLOR SCIENCES INTERNATIONAL INC
Form 10-Q
August 20, 2001

SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended June 30, 2001

OR

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

For the transition period from _________ to _________

Commission file number 0-21168

CHROMATICS COLOR SCIENCES INTERNATIONAL, INC.
(Exact Name of Registrant as Specified in Its Charter)

New York	13-3253392
(State or Other Jurisdiction of Incorporation or Organization)	(I.R.S. Employer Identification Number)

5 East 80th Street, New York, New York 10021
(Address of principal executive offices)

(212) 717-6544
(Registrant's Telephone Number, Including Area Code)

n/a
(Former Name, Former Address and Former Fiscal Year, if Changed Since Last Report)

Indicate by check whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes [X] No [ ]

APPLICABLE ONLY TO ISSUERS INVOLVED IN BANKRUPTCY PROCEEDINGS DURING THE PRECEDING FIVE YEARS:

Indicate by check whether the registrant has filed all documents and reports required to be filed by Section 12, 13 or 15(d) of the Securities Exchange Act of 1934 subsequent to the distribution of securities under a plan confirmed by court. Yes [ ] No [ ] N/A

APPLICABLE ONLY TO CORPORATE ISSUERS:

Indicate the number of shares outstanding of each of the registrant's classes of common stock, as of August 15, 2001: 19,991,952

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PART I -- FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

CHROMATICS COLOR SCIENCES INTERNATIONAL, INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS

	June 30, 2001 (unaudited)	December 31, 2000 (Notes 1 and 3)
ASSETS		
CURRENT ASSETS:		
Cash and equivalents	$ 69,400	$ 1,379,000
Accounts receivable	72,900	72,900
Inventories	720,900	747,100
Prepaid expenses and other current assets	80,500	296,900
Deferred financing costs	472,000	-
Total Current Assets	1,415,700	2,495,900
PROPERTY AND EQUIPMENT - NET	202,300	244,100
SOFTWARE DEVELOPMENT COSTS - NET	156,800	261,400
PATENT COSTS - NET	530,800	581,100
NET ASSETS OF DISCONTINUED OPERATIONS	-	1,000,000
OTHER ASSETS	306,600	331,700
	$ 2,612,200	$ 4,914,200
LIABILITIES AND STOCKHOLDERS' EQUITY		
CURRENT LIABILITIES:		
Accounts payable and accrued expenses:		
Attorneys and accountants	$ 923,300	$ 458,900
Consultants	249,600	141,700
Trade	385,800	260,100
Severance payable	700,000	
Reserve for notes payable (including $341,000 payable to an affiliate)	760,000	-

	3,018,700	860,700
LONG TERM DEBT:		
Amount payable for purchase of Gordon	-	653,000
	-	653,000
COMMITMENTS AND CONTINGENCIES		
REDEEMABLE PREFERRED STOCK:		
Class A, Par Value $.01 per share:		
Authorized - 1,400,000 shares		
Issued and outstanding - 1,380,000 shares at par value and redemption value	13,800	13,800
	13,800	13,800
SHAREHOLDERS' EQUITY (DEFICIENCY)		
Preferred Stock	12,066,800	11,510,800
Common Stock, par value $.001 per share:		
Authorized - 50,000,000 shares		
Issued and outstanding - 19,991,952 (2001) and 19,033,308 (2000) shares	20,000	19,100
Capital in excess of par value	46,596,500	45,934,400
Accumulated deficit	(59,103,600)	(54,077,600)
Total Shareholders' Equity (Deficiency)	(420,300)	3,386,700
	$ 2,612,200	$ 4,914,200

See accompanying notes to consolidated financial statements

CHROMATICS COLOR SCIENCES INTERNATIONAL, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF OPERATIONS
(UNAUDITED)

	Three Months Ended June 30,		Six Months En
	2001	2000	2001
Revenues:			
Sales	$ -	$ 41,100	$ -
COSTS AND EXPENSES:			
Cost of sales		6,100	-
Sales, marketing and trade show costs	9,600	533,300	253,400
Medical regulatory expenses	1,900	227,200	278,300
Research and development	149,600	380,200	454,700
Patent application costs	35,700	94,400	171,700
Compensation costs relating to (noncash) options granted	-	225,000	-
Provision for estimated payments for			

terminated employees	-	-	1,000,000
General and administrative:			
Compensation-Officers, employees and consultants	250,000	395,300	654,300
Legal fees	45,800	250,900	200,200
Accounting fees	22,900	26,700	62,900
Rent and storage	96,100	78,900	188,500
Insurance	51,300	71,800	123,800
Repairs and maintenance	9,400	34,800	30,300
Depreciation and amortization	126,100	173,000	252,100
Taxes	20,400	20,000	56,200
Stock administrative fees	30,700	24,900	60,400
Public relations	700	52,800	40,200
Other	45,500	108,000	102,800
	895,700	2,703,300	3,929,800
OPERATING LOSS	(895,700)	(2,662,200)	(3,929,800)
OTHER INCOME(EXPENSE):			
Interest income		45,000	2,800
Interest expense and non-cash financing costs including $94,000 and $834,200 in non-cash OID costs in 2001 and 2000, respectively	(99,000)	(300,800)	(99,000)
	(99,000)	(255,800)	(96,200)
LOSS FROM CONTINUING OPERATIONS	(994,700)	(2,918,000)	(4,026,000)
LOSS FROM DISCONTINUED OPERATIONS(Note3)		(41,100)	(1,000,000)
NET LOSS	$ (994,700)	$ (2,959,100)	$ (5,026,000)
NET LOSS TO COMMON STOCKHOLDERS:			
LOSS FROM CONTINUING OPERATIONS	$ (994,700)	$ (2,918,000)	$ (4,026,000)
DEEMED DIVIDEND FOR CLASS B, SERIES 2 AND 3 CONVERTIBLE PREFERRED STOCK	278,000	278,000	556,000
LOSS FROM CONTINUING OPERATIONS TO COMMON STOCKHOLDERS	(1,272,700)	(3,196,000)	(4,582,000)
LOSS FROM DISCONTINUED OPERATIONS(Note3)	-	(41,100)	(1,000,000)
NET LOSS TO COMMON SHAREHOLDERS	$ (1,272,700)	$ (3,237,100)	$ (5,582,000)
WEIGHTED AVERAGE NUMBER OF COMMON SHARES OUTSTANDING	19,538,268	16,183,925	19,285,788
BASIC AND DILUTED LOSS PER SHARE:			
LOSS FROM CONTINUING OPERATIONS	$ (0.07)	$ (0.20)	$ (0.24)
LOSS FROM DISCONTINUED OPERATIONS	-	-	(0.05)
NET LOSS TO COMMON STOCKHOLDERS	$ (0.07	$ (0.20)	$ (0.29)

See accompanying notes to consolidated financial statements

CHROMATICS COLOR SCIENCES INTERNATIONAL, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENT OF CHANGES IN STOCKHOLDERS' EQUITY (DEFICIENCY)
(UNAUDITED)

		Common Stock		
	Preferred Stock	Number of Shares Outstanding	Par Value	Capital i Excess of P Value
Balances, December 31, 2000	$ 11,510,800	19,033,308	$ 19,100	$ 45,934,4
Six Months Ended June 30, 2001:				
Net Loss	-	-	-	
Issuance of common stock - Gordon	-	22,894	-	653,0
Issuance of common stock - private investor	-	935,750	900	(9
Warrants issued in connection with bridge notes	-	-	-	566,0
Deemed dividend on Class B, convertible preferred stock	556,000	-	-	(556,0
Balances, June 30, 2001	$ 12,066,800	19,991,952	$ 20,000	$ 46,596,5

See accompanying notes to consolidated financial statements

CHROMATICS COLOR SCIENCES INTERNATIONAL, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
(UNAUDITED)

	Three Months Ended June 30	
	2001	2000

CASH FLOWS FROM OPERATING ACTIVITIES:		
Loss from continuing operations	$(4,026,000)	$(6,346,700
Loss from discontinued operations	(1,000,000)	--
Adjustments to reconcile net loss to net cash flows from operating activities:		
Non-cash impairment charge and net change in net assets of discontinued operations	1,000,000	--
Depreciation and amortization	252,100	344,400
Compensation cost relating to options granted to consultants	--	465,000
Non-cash interest and financing costs	94,000	834,200
Changes in operating assets and liabilities:		
Accounts receivable	--	767,600
Inventories	(26,100)	(191,400
Prepaid expenses and other assets	241,500	(25,000
Accrued interest on senior convertible debentures	--	350,000
Accounts payable and accrued expenses	1,698,000	(41,600
Net cash flows from continuing operating activities	(1,766,500)	(3,843,500
CASH FLOWS FROM INVESTING ACTIVITIES:		
Capitalized patent costs	--	(255,100
Net cash used for investment in subsidiary	--	(1,263,100
Purchase of property and equipment	(3,100)	(61,900
Net cash flows from investing activities	(3,100)	(1,580,100
CASH FLOWS FROM FINANCING ACTIVITIES:		
Proceeds from issuance of common stock, net of related costs	--	795,200
Proceeds (payments) of Notes payable	460,000	(12,800
Net proceeds from the issuance of preferred stock and warrants, net of costs	--	3,610,000
Net cash flows from financing activities	460,000	4,392,400
NET CHANGE IN CASH AND EQUIVALENTS	(1,309,600)	(1,031,200
CASH AND EQUIVALENTS, BEGINNING OF PERIOD	1,379,000	2,790,400
CASH AND EQUIVALENTS, END OF PERIOD	$ 69,400	$ 1,759,200
SUPPLEMENTAL CASH FLOW INFORMATION		
Interest Paid	$ --	$ 43,500
Issuance of debt to pay accrued expenses	$ 300,000	$ --
Issuance of stock to pay Gordon liability	653,000	--
Deemed dividends	556,000	981,000

See accompanying notes to consolidated financial statements

CHROMATICS COLOR SCIENCES INTERNATIONAL, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 1 - Basis of Presentation:

Nature of Report - The consolidated balance sheet at the end of the preceding fiscal year has been derived from the audited consolidated balance sheet contained in the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2000 and is presented for comparative purposes. All other financial statements are unaudited. In the opinion of management, all adjustments, which include only normal recurring adjustments necessary to present fairly the financial position, results of operations and changes in cash flows, for all periods presented have been made. The results of operations for interim periods are not necessarily indicative of the operating results for the full year.

Footnotes - Certain footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles have been omitted in accordance with the published rules and regulations of the Securities and Exchange Commission. These consolidated financial statements should be read in conjunction with the financial statements and notes thereto included in the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2000.

Note 2 - Commitments and Contingencies:

Business Risks - Since its formation in 1984, the Company has been principally engaged in color science technology research and development and licensing activities, seeking mass market applications for its proprietary technology and instrumentation. The Company's business encompasses all of the risks inherent in the establishment of a new business enterprise, including a limited operating history with significant competition possessing substantially greater resources. Current and future operations also depend upon the continued employment of certain key executives, the ability to further commercialize its proprietary technology and products and the Company's ability to obtain sufficient revenues and outside financing.

Operating Difficulties - Since 1989, the Company has incurred losses from operations and net cash outflows from operations. The Company expects to license its patents and proprietary technology, sell its equipment and market its related services and products to ultimately overcome these difficulties.

Although the Company has taken steps to substantially reduce personnel and ongoing operating expenses, the Company expects that it will continue to incur costs in connection with the required research and development on its new LED instrument and technology, complete filings, administration and maintenance for certain intellectual properties and regulatory requirements; supply updated products and sales support to its medical distributor; complete FDA filings for upgrades to its medical products, and explore the possibility of either renegotiating its current distribution agreement for its medical products or selling the exclusive rights to its medical products and technology. There can be no assurance the Company will not continue to incur such losses or will ever generate revenues at levels sufficient to support profitable operations.

The Company anticipates that it will continue to incur net losses for the foreseeable future as expenses are incurred in implementing its long-term business plan.

The Company is currently taking steps to improve operating results and has initiated a plan to significantly reduce operating costs. The Company is experiencing a major liquidity crisis and requires an immediate infusion of cash to continue operations. The Company is seeking additional capital to facilitate short-term liquidity and is currently reviewing various financing proposals. If the Company is unable to obtain such short-term financing, or sell its assets to obtain a cash infusion, it may be forced to seek protection from its creditors in bankruptcy.

Even if the Company is successful in obtaining this short-term cash infusion, the Company will require additional future financing to execute its business plan. If the Company is not able to attract additional future financing, generate significant revenue from operations and/or successfully market its products and technologies, it may have to significantly curtail and/or cease operations and be forced to seek protection from its creditors in bankruptcy.

In addition, on May 29, 2001, the Company received a determination letter from the staff of the Nasdaq Stock Market that the Company fails to comply with the net tangible assets/market capitalization/ net income requirement for continued listing set forth in Nasdaq's Marketplace Rules 4310(c)(2)(B). Further, the Company was notified by letter dated July 3, 2001 by the Hearings Department that the net tangible assets deficiency would be considered a basis for delisting at the Company's hearing before the Nasdaq Listing Qualifications Panel (the "Panel") which took place on August 16, 2001. The net tangible assets/market capitalization/ net income deficiency was a subject of the Company's hearing. The Company's hearing has stayed the delisting of the Company's securities pending the Panel's decision. NASDAQ has requested more information from the Company. There can be no assurance that the Qualifications Panel will grant the Company's request for continued listing.

Legal Proceedings - On January 16, 2001, a lawsuit was commenced against the Company and Darby Macfarlane in the federal district court for the Southern District of New York entitled Richard Sommers and Linda Sommers v. Chromatics Color Sciences International, Inc. and Darby S. Macfarlane. The plaintiffs allege that certain statements purportedly made by or on behalf of the Company concerning the Company's success, the extent of use of the ColorMate (Registered Trademark) System and the Company's cash flow constituted violations of Section 10(b) of the Securities Exchange Act of 1934 and SEC Rule 10b-5 promulgated thereunder and Section 12(a)(2) of the Securities Act of 1933 as well as common law claims alleging fraudulent misrepresentation, concealment and nondisclosure and seek unspecified damages in an amount to be proven at trial. On March 1, 2001, the defendants moved to dismiss the complaint for failure to state a claim upon which relief can be granted, for failure to plead fraud with requisite particularity and for failure to comply with the statutory requirements for federal securities fraud claims. No decision has been rendered by the court on this motion. The defendants believe that the allegations of the complaint are without merit and intend to vigorously defend this action.

Note 3 - Discontinued Operations:

On June 2, 2000, the Company purchased Gordon Laboratories, Inc. ("Gordon"). Due to the recent financial results of Gordon and CCSI's inability to continue funding Gordon, the Company decided to sell Gordon in the first quarter of 2001. On July 3, 2001 the Company completed the sale of Gordon (see below). The Company retains the right to repurchase Gordon within the one year anniversary of July 3, 2001. Accordingly, results of this operation have been classified as discontinued, and prior periods have been restated. The net assets of Gordon were written-down to zero as of March 31, 2001.

In connection with the purchase of Gordon, the Company was required to issue additional shares of its common stock to certain Gordon options holders on June 2, 2001 at a price of $6.29 per share. In accordance with this provision, the Company issued 22,894 shares on July 3, 2001. The financial statements reflect these shares as if they had been fully issued on June 2, 2001.

Net sales and loss from the discontinued operation are as follows:

	Three months ended	Six months ended	Three months ended
	June 30, 2001		June 3
Net Sales	$ 1,423,000	$ 2,590,000	$ 626,200
Loss from discontinued operation	$ 549,000	$ 1,000,000	$ 41,100
Impairment cost (gain)	$ (549,000)*	$ 0	$ 0
Net Loss from discontinued operation	$ 0	$ 1,000,000	$ 41,100

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* Note - Gordon's net assets were written-down to zero at March 31, 2001. Losses subsequent to March 31, 2001 at Gordon had no effect on the Company's financial statements.

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Assets and liabilities from the discontinued operation were as follows:

	December 31, 2000
Current assets	$ 1,821,500
Property and equipment/other assets	$ 3,261,100
Current liabilities	$ 4,082,600
Long-term liabilities	$ 0
Net assets of discontinued operation	$ 1,000,000

Sale of Gordon

On July 3, 2001, pursuant to the Share Subscription and Redemption Agreement, dated as of June 19, 2001 (the "Purchase Agreement"), among the Company, Abilene Investments Corp. ("Abilene"), GAC-Labs, LLC ("GAC- Labs" and collectively with Abilene, the "Purchasers") and Gordon Acquisition Corp., a wholly-owned subsidiary of the Company ("Gordon"), Gordon issued 200 shares of common stock, par value $.001 per share, of Gordon ("Gordon Stock") to Abilene and 800 shares of Gordon Stock to GAC-Labs for an aggregate purchase price of $1,000,000. Simultaneously, the shares of Gordon Stock that were outstanding immediately prior to the closing of this transaction, all of which were owned by the Company, were redeemed for one dollar. In addition, the Company assigned to the Purchasers its right, title and interest in the indebtedness of Gordon and/or H.B. Gordon Manufacturing Co., Inc., its wholly-owned subsidiary, owed to the Company in the ratio of 20% to Abilene and 80% to GAC-Labs.

As part of the same transaction, pursuant to the Purchase Option Agreement, dated as of July 3, 2001 (the "Option Agreement"), among the Company, Abilene and GAC-Labs, the Company was granted the option to purchase from the Purchasers the shares of Gordon Stock issued to them and the indebtedness assigned to them under the Purchase Agreement within one year for an aggregate purchase price of $1,000,000 plus interest thereon at the rate of 14% per annum, subject to reduction under certain conditions, as described below.

Furthermore, the Company granted to the Purchasers one-year warrants (the "Warrants") to purchase (i) an aggregate of 2,000,000 shares of common stock, par value $.001 per share, of the Company ("CCSI Stock") at the exercise price of $.50 per share, if the Company does not consummate a rights offering/ private placement by the Company of its securities prior to the one year expiration of such warrants, or alternatively (ii) an aggregate of 11,200,000 shares of CCSI Stock at the exercise price of $.10 per share and 4.8 million shares at $0.001 per share, subject to price adjustment, if the Company consummates a rights offering/private placement by the Company of its securities prior to the one year expiration of such warrants and obtains shareholder approval with respect to such rights offering/private placement by the Company of its securities and such increase in warrants. The fair market value of the 2 million warrants was immaterial. If the alternative additional warrants are issued at a later date, the fair market value of such warrants will be recorded as a further loss on the disposal of Gordon.

If (i) pursuant to the Option Agreement the Company exercises its option to purchase from the Purchasers the shares of Gordon Stock issued to them and the indebtedness assigned to them under the Purchase Agreement, (ii) the Company has not effected a reverse stock split of the CCSI Stock in a ratio greater than ten to one, (iii) the Company has consummated a rights offering/private placement by the Company of its securities and (iv) the market price of CCSI Stock exceeds $1.00 per share for at least ten consecutive trading days from and after the date of exercise under the Option Agreement, the Warrants will be subject to mandatory exercise. In the event of such a mandatory exercise, the Company will accept as payment of the aggregate exercise price the shares of Gordon Stock that the Purchasers acquired under the Purchase Agreement, and the exercise price under the Option Agreement will be reduced to one dollar. The Warrants are also subject to mandatory exercise if (i) a registration statement filed by the Company with respect to the shares of CCSI Stock issuable upon exercise of the Warrants has been declared effective by the Securities and Exchange Commission, (ii) the Company has not effected a reverse stock split of the CCSI Stock in a ratio greater than ten to one, (iii) the Company has consummated a rights offering/private placement by the Company of its securities and (iv) the market price of CCSI Stock exceeds $1.00 per share for at least ten consecutive trading days from and after the effective date of such registration statement. In the event of such a mandatory exercise, the Company will accept payment of the aggregate exercise price through the means of a broker's cashless exercise transaction.

Note 4 - Issuance of Common Stock:

In connection with an "adjustable warrant" granted to a private investor in 2000, the Company issued 935,750 shares of its common stock to such investor as a result of the first adjustment of such warrant which occurred on March 31, 2001.

In connection with the purchase of Gordon, the Company issued 22,894 of its common shares in July 2001. See Note 3.

Note 5 - Employee termination payments

Since March 2001, the Company terminated many of its employees or has been unable to pay many of its existing employees. Some of these employees have employment contracts that provide for severance and other payments upon the termination of employment or breach in such contracts. Accordingly, the Company has recorded a $1,000,000 provision for the estimated exposure to these employees for additional amounts due to them. As of June 30, 2001, $300,000 of this provision has been utilized via payments by an officer of the Company. The Company believes the remaining $700,000 accrual is reasonable.

Note 6 - Notes payable

During the quarter ended June 30, 2001 the Company received $760,000 through the issuance of bridge notes ($300,000 resulted from the payment by an officer of Company liabilities). The notes bear interest at a fixed rate of 10% and are due in one year. In connection with the debt, the Company issued an aggregate of 5 million warrants which vest immediately, have a five year life and are exercisable at $0.10 per share. The fair market value of these warrants amounted to $566,000 determined using the Black-Scholes option pricing model. The fair market value of these warrants issued in connection with debt has been recorded as deferred financing costs, is included in current assets, and is being amortized over the life of the relative debt. For the six months ended June 30, 2001, approximately $94,000 was charged to non-cash financing costs relating to the amortization of the deferred financing costs.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

RESULTS OF OPERATIONS

The Company incurred losses from continuing operations of $994,700 and $2,918,000 for the three months ended June 30, 2001 and 2000, respectively. For the six months ended June 30, 2001 and 2000, the Company incurred losses from continuing operations of $4,026,000 and $6,346,700, respectively. Loss per share from continuing operations for the three months ended June 30, 2001 and 2000 were ($.07) and ($.20), respectively. Loss per share from continuing operations for the six months ended June 30, 2001 and 2000 were ($.24) and ($.46), respectively. The reduction in losses incurred from continuing operations is primarily attributable to the Company's ability to reduce its operating costs in accordance with its business plan.

The Company incurred losses from Discontinued Operations of $1,000,000 or ($.05) per share for the six months ended June 30, 2001 and $41,100 or ($.0) per share for the three and six months ended June 30, 2000 due to the decision to dispose of the Gordon operation (See Note 3).

Sales, marketing and trade show costs were $9,600 and $253,400 for the three and six months ended June 30, 2001 as compared to $533,300 and $1,170,700 in the prior periods as the Company has substantially reduced its medical sales force in 2001. Medical regulatory expenses were $1,900 and $278,300 for the three and six months ended June 30, 2001 as compared to $227,200 and $423,600 in the prior periods due to significant reductions in the second quarter of 2001 in FDA filing costs relating to medical products and other regulatory requirements.

Research and development costs were $149,600 for the three months ended June 30, 2001 as compared to $380,200 for the three months ended June 30, 2000. The decrease in research and development costs in the current period is primarily a result of completion of certain milestones in development of the Company's medical product. Research and development costs were $454,700 for the six months ended June 30, 2001 as compared to $674,900 for the six months ended June 30, 2000. The decreased research and development costs for the six months ended June 30,2001 are primarily a result of the above-mentioned completion of milestones.

The Company recorded a provision for estimated payments for terminated employees of $1,000,000 at March 31, 2001.

Compensation costs - Officers, employees and consultants were $250,000 for the three months ended June 30, 2001 as compared to $395,300 for the three months ended June 30, 2000. The decrease in these costs in the current period is a result of the Company's significant decreases in personnel in 2001. Officers, employees and consultants were $654,300 for the six months ended June 30, 2001 as compared to $739,700 for the six months ended June 30, 2000. The decreases were caused by the same reasons.

Total General and administrative costs were $698,900 and $1,768,700 for the three and six months ended June 30, 2001 as compared to $1,237,100 and $2,407,300 in the prior periods. The decrease is primarily a result of cost reductions initiated by the Company in 2001.

Interest and non-cash financing costs were $99,000 in the three and six months ended June 30, 2001 as compared to $300,800 and $1,197,400 in the prior periods. The decrease is primarily due to amortization of original issue discount on senior convertible debentures, which was fully amortized in prior periods.

Deemed dividends on preferred stock were $278,000 and $556,000 in the three and six months ended June 30, 2001 as compared to $278,000 and $981,000 in the prior periods. The decrease for the six month period is due to an additional deemed dividend from a new financing in the prior period, which did not occur in the current period.

Although the Company has substantially reduced personnel and ongoing operating expenses, the Company expects that if it is successful in raising the necessary financing to continue operations, it will continue to incur costs in connection with the required research and development for different market applications of its new LED instrument and technology, complete filings, administration and maintenance for certain intellectual properties and regulatory requirements; supply updated products and sales support to its medical distributor; complete FDA filings for upgrades to its medical products, and explore the possibility of either renegotiating its current distribution agreement for its medical products or selling the exclusive rights to its medical products and technology.

The Company anticipates that it will continue to incur net losses for the foreseeable future as expenses are incurred in implementing its long-term business plan.

LIQUIDITY AND CAPITAL RESOURCES

Current Assets were $1,415,700 at June 30, 2001 as compared to $2,495,900 at December 31, 2000. This decrease is primarily attributable to a decrease in cash due to the operating losses.

As indicated in the Consolidated Statement of Cash Flows, the Company continues to experience significant negative net cash flows from operating activities. The 2001 net cash outflow from operating activities is primarily attributed to the Company's net loss partially offset by depreciation and amortization expense and increases in accounts payable.

The Company lacks funds to continue material aspects of its operations and business plan, including funds and necessary personnel to complete research and development on its new LED instrument and technology recently required during its first mass manufacturing process; complete filings, administration and maintenance for certain intellectual properties and regulatory requirements; supply upgraded products and sales support to its medical distributor; and complete FDA regulatory filings for upgrades to its medical products.

The Company's current objective with regard to its medical business is to arrive at acceptable revised terms of the existing agreement with the distributor or to identify a strategic partner in the medical industry to whom the Company

could sell, for an up-front fee and ongoing royalty, the exclusive market rights to the ColorMate(R) TLc-BiliTest(R) System.

The Independent Accountants' Report on the December 31, 2000 financial statements indicates the Company has incurred recurring losses for the last several years, including $19,464,400 in 2000 and has experienced significant problems and delays exploiting its primary technology (medical equipment). In addition, the Company's subsidiary, Gordon, defaulted on its debt services obligations and the lender demanded payment of the entire debt, which totaled $2,714,700 at December 31, 2000. The Independent Accountants' Report states that these matters raise substantial doubt about the Company's ability to continue as a going concern. Gordon has subsequently been sold. See Note 3.

The Company is experiencing a major liquidity crisis and requires an immediate infusion of cash to continue operations. The Company is seeking additional capital to facilitate short-term liquidity and is currently reviewing various financing proposals and has taken steps to significantly reduce costs. If the Company is unable to obtain such short-term financing, or sell its assets to obtain a cash infusion, it may be forced to seek protection from its creditors in bankruptcy.

Even if the Company is successful in obtaining this short-term cash infusion, the Company will require additional future financing to execute its business plan. If the Company is not able to attract additional future financing, generate significant revenue from operations and/or successfully market its products and technologies, it may have to significantly curtail and/or cease operations and be forced to seek protection from its creditors in bankruptcy.

The Company is currently negotiating proposals for financing the Company. Such proposals require negotiation of warrants to purchase the Company's stock and are subject to satisfactory completion of due diligence, negotiation, execution and delivery of definitive agreements by and between the parties, and compliance with NASDAQ listing requirements.

Some of the information presented in or incorporated by reference in this report constitutes "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995. Although the Company believes that its expectations are based on reasonable assumptions, within the bounds of its knowledge of its business and operations, there can be no assurance that actual results will not differ materially from its expectations. Factors that could cause actual results to differ from expectations include, among other things: (i) the inability of the Company to resolve the current liquidity crisis, (ii) the inability of the Company to secure additional financing, (iii) the failure of the Company to implement its business plan for various applications of its technologies, including medical and industrial technologies, (iv) government regulation and (v) the loss of key personnel.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

No disclosure is required under this Item 3.

PART II - OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

On January 16, 2001, a lawsuit was commenced against the Company and Darby Macfarlane in the federal district court for the Southern District of New York entitled Richard Sommers and Linda Sommers v. Chromatics Color Sciences International, Inc. and Darby S. Macfarlane. The plaintiffs allege that certain statements purportedly made by or on behalf of the Company concerning the Company's success, the extent of use of the ColorMate (Registered Trademark) System and the Company's cash flow constituted violations of Section 10(b) of the Securities Exchange Act of 1934 and SEC Rule 10b-5 promulgated thereunder and Section 12(a)(2) of the Securities Act of 1933 as well as common law claims alleging fraudulent misrepresentation, concealment and nondisclosure and seek unspecified damages in an amount to be proven at trial. On March 1, 2001, the defendants moved to dismiss the complaint for failure to state a claim upon which relief can be granted, for failure to plead fraud with requisite particularity and for failure to comply with the statutory requirements for federal securities fraud claims. No decision has been rendered by the court on this motion. The defendants believe that the allegations of the complaint are without merit and intend to vigorously defend this action.

ITEM 2. CHANGES IN SECURITIES AND USE OF PROCEEDS.

None.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES.

None.

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

None.

ITEM 5. OTHER INFORMATION.

None.

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K.

Reports on Form 8-K:

None.

SIGNATURES

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

CHROMATICS COLOR SCIENCES INTERNATIONAL, INC.

Date: August 20, 2001 By: /s/ Darby S. Macfarlane

Darby S. Macfarlane
Chairman and Chief Technology Officer

Date: August 20, 2001 By: /s/ Leslie Foglesong
Leslie Foglesong
Asst. Treasurer and principal
accounting officer