

SAFEGUARD SCIENTIFICS INC

Form 10-Q

May 11, 2009

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**SECURITIES AND EXCHANGE COMMISSION**  
**Washington, DC 20549**  
**FORM 10-Q**  
**Quarterly Report Pursuant to Section 13 or 15(d)**  
**of the Securities Exchange Act of 1934**  
**For the Quarter Ended March 31, 2009**  
**Commission File Number 1-5620**  
**Safeguard Scientifics, Inc.**  
**(Exact name of registrant as specified in its charter)**

**Pennsylvania**  
*(State or other jurisdiction of  
incorporation or organization)*

**23-1609753**  
*(I.R.S. Employer ID No.)*

**435 Devon Park Drive**  
**Building 800**  
**Wayne, PA**  
*(Address of principal executive offices)*

**19087**  
*(Zip Code)*

**(610) 293-0600**

**Registrant's telephone number, including area code**

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15 (d) of the Securities and Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports) and (2) has been subject to such filing requirements for the past 90 days. Yes  No   
Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes  No

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

Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting  
company

(Do not check if a smaller  
reporting company)

Indicate by check mark whether the Registrant is a shell company (as defined in Exchange Act Rule 12b-2). Yes  No

**Number of shares outstanding as of May 8, 2009**  
**Common Stock 122,029,312**

**SAFEGUARD SCIENTIFICS, INC.**  
**QUARTERLY REPORT ON FORM 10-Q**  
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**SAFEGUARD SCIENTIFICS, INC.  
CONSOLIDATED BALANCE SHEETS**

|   | <b>March 31,<br/>2009</b>                                   | <b>December 31,<br/>2008</b> |
|---|---|------------------------------|
|   | <b>(In thousands except per share data)<br/>(unaudited)</b> |                              |
| <b>ASSETS</b>   |   |                              |
| Current Assets:   |   |                              |
| Cash and cash equivalents   | \$ 89,049   | \$ 75,051                    |
| Cash held in escrow and restricted cash   | 7,747   | 6,433                        |
| Marketable securities   | 6,434   | 14,701                       |
| Restricted marketable securities  |   | 1,990                        |
| Accounts receivable, less allowances (\$7,173 2009; \$8,045 2008)   | 25,486  | 20,465                       |
| Prepaid expenses and other current assets   | 3,345   | 1,507                        |
| <br>  |   |                              |
| Total current assets  | 132,061   | 120,147                      |
| Property and equipment, net   | 14,240  | 12,369                       |
| Ownership interests in and advances to companies  | 82,929  | 85,561                       |
| Goodwill  | 12,729  | 12,729                       |
| Cash held in escrow and restricted cash   | 1,976   | 501                          |
| Other   | 1,088   | 1,095                        |
| <br>  |   |                              |
| Total Assets  | \$ 245,023  | \$ 232,402                   |
| <b>LIABILITIES AND SHAREHOLDERS EQUITY</b>  |   |                              |
| Current Liabilities:  |   |                              |
| Current portion of credit line borrowings   | \$ 5,887  | \$ 14,104                    |
| Current maturities of long-term debt  | 607   | 263                          |
| Accounts payable  | 4,098   | 3,337                        |
| Accrued compensation and benefits   | 4,334   | 5,758                        |
| Accrued expenses and other current liabilities  | 8,169   | 8,285                        |
| <br>  |   |                              |
| Total current liabilities   | 23,095  | 31,747                       |
| Long-term debt  | 1,152   | 345                          |
| Other long-term liabilities   | 9,302   | 9,600                        |
| Convertible senior debentures   | 86,000  | 86,000                       |
| <br>  |   |                              |
| Commitments and contingencies   |   |                              |
| <br>  |   |                              |
| Shareholders Equity:  |   |                              |
| Preferred stock, \$0.10 par value; 1,000 shares authorized  |   |                              |
| Common stock, \$0.10 par value; 500,000 shares authorized; 122,029 and 121,589 shares issued and outstanding in 2009 and 2008, respectively | 12,203  | 12,159                       |
| Additional paid-in capital  | 777,357   | 763,323                      |
| Accumulated deficit   | (678,952)   | (669,526)                    |
| Accumulated other comprehensive income (loss)   | (28)  | (29)                         |
| Treasury stock, at cost   |   | (1,217)                      |

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|  |            |            |
|--|------------|------------|
| Total Safeguard Scientifics, Inc. shareholders' equity | 110,580    | 104,710    |
| Noncontrolling interest in subsidiary                  | 14,894     |            |
| Total shareholders' equity                             | 125,474    | 104,710    |
| Total Liabilities and Shareholders' Equity             | \$ 245,023 | \$ 232,402 |

See Notes to Consolidated Financial Statements.

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**SAFEGUARD SCIENTIFICS, INC.**  
**CONSOLIDATED STATEMENTS OF OPERATIONS**

|  | <b>Three Months Ended March 31,</b>         |             |
|--|---|-------------|
|  | <b>2009</b>                                 | <b>2008</b> |
|  | <b>(In thousands except per share data)</b> |             |
|  | <b>(Unaudited)</b>                          |             |
| Revenue  | \$ 22,447                                   | \$ 15,886   |
| Operating Expenses:  |   |             |
| Cost of sales  | 8,966                                       | 7,397       |
| Selling, general and administrative  | 17,009                                      | 13,956      |
| Total operating expenses   | 25,975                                      | 21,353      |
| Operating loss   | (3,528)                                     | (5,467)     |
| Other income (loss), net   | (245)                                       | 360         |
| Recovery related party   |   | 1           |
| Interest income  | 157   | 929         |
| Interest expense   | (926)                                       | (1,374)     |
| Equity loss  | (5,513)                                     | (6,614)     |
| Net loss from continuing operations before income taxes  | (10,055)                                    | (12,165)    |
| Income tax (expense) benefit   |   |             |
| Net loss from continuing operations  | (10,055)                                    | (12,165)    |
| Income (loss) from discontinued operations, net of tax   | 1,500                                       | (7,078)     |
| Net loss   | (8,555)                                     | (19,243)    |
| Net (income) loss attributable to noncontrolling interest  | (871)                                       | 389         |
| Net loss attributable to Safeguard Scientifics, Inc.   | \$ (9,426)                                  | \$ (18,854) |
| Basic and Diluted Income (Loss) Per Share:   |   |             |
| Net loss from continuing operations attributable to Safeguard Scientifics, Inc. common shareholders            | \$ (0.08)                                   | \$ (0.10)   |
| Net income (loss) from discontinued operations attributable to Safeguard Scientifics, Inc. common shareholders |   | (0.05)      |
| Net loss attributable to Safeguard Scientifics, Inc. common shareholders                                       | \$ (0.08)                                   | \$ (0.15)   |
| Shares used in computing basic and diluted income (loss) per share   | 121,645                                     | 122,996     |
| Amounts attributable to Safeguard Scientifics, Inc. common shareholders:                                       |   |             |
| Loss from continuing operations  | \$ (10,321)                                 | \$ (11,778) |

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|  |            |             |
|--|------------|-------------|
| Income (loss) from discontinued operations           | 895        | (7,076)     |
| Net loss attributable to Safeguard Scientifics, Inc. | \$ (9,426) | \$ (18,854) |

See Notes to Consolidated Financial Statements.

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**SAFEGUARD SCIENTIFICS, INC.**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**

|   | <b>Three Months Ended March 31,</b> |             |
|---|-------------------------------------|-------------|
|   | <b>2009</b>                         | <b>2008</b> |
|   | <b>(In thousands)</b>               |             |
|   | <b>(Unaudited)</b>                  |             |
| <b>Cash Flows from Operating Activities:</b>  |                                     |             |
| Cash flows from operating activities of continuing operations   | \$ (6,816)                          | \$ (3,437)  |
| Cash flows from operating activities of discontinued operations   |                                     | (2,871)     |
| Net cash used in operating activities   | (6,816)                             | (6,308)     |
| <b>Cash Flows from Investing Activities:</b>  |                                     |             |
| Advances to partner companies   | (250)                               |             |
| Acquisitions of ownership interests in partner companies and funds, net of cash acquired  | (3,268)                             | (2,841)     |
| Repayment of note receivable-related party, net   |                                     | 1           |
| Increase in marketable securities   | (5,783)                             | (2,224)     |
| Decrease in marketable securities   | 14,050                              | 296         |
| Increase in restricted cash, net  | (1,953)                             |             |
| Capital expenditures  | (1,783)                             | (1,550)     |
| Cash flows from investing activities of discontinued operations   |                                     | (2,091)     |
| Net cash provided by (used in) investing activities   | 1,013                               | (8,409)     |
| <b>Cash Flows from Financing Activities:</b>  |                                     |             |
| Borrowings on revolving credit facilities   | 15,945                              | 10,543      |
| Repayments on revolving credit facilities   | (24,162)                            | (15,540)    |
| Borrowings on term debt   |                                     | 322         |
| Repayments on term debt   | (64)                                | (2,419)     |
| Issuance of subsidiary equity, net  | 28,082                              | 217         |
| Cash flows from financing activities of discontinued operations   |                                     | (216)       |
| Net cash provided by (used in) financing activities   | 19,801                              | (7,093)     |
| Net Increase (Decrease) in Cash and Cash Equivalents  | 13,998                              | (21,810)    |
| Changes in Cash and Cash Equivalents from, and advances to Acsis, Alliance Consulting and Laureate Pharma included in assets of discontinued operations |                                     | 1,019       |
|   | 13,998                              | (20,791)    |
| Cash and Cash Equivalents at beginning of period  | 75,051                              | 96,201      |
| Cash and Cash Equivalents at end of period  | \$ 89,049                           | \$ 75,410   |



See Notes to Consolidated Financial Statements.

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**SAFEGUARD SCIENTIFICS, INC.**  
**CONSOLIDATED STATEMENT OF SHAREHOLDERS EQUITY**  
(In thousands)  
(Unaudited)

| Safeguard Scientifics, Inc. Shareholders |             |              |         |         |           |            |        |                |        |
|--|-------------|--------------|---------|---------|-----------|------------|--------|----------------|--------|
| Accumulated                              |             |              |         |         |           |            |        |                |        |
| Other                                    |             |              |         |         |           |            |        |                |        |
| Comprehensive                            |             |              |         |         |           |            |        |                |        |
| Additional                               |             |              |         |         |           |            |        |                |        |
| Total                                    | Accumulated | Income       | Common  | Stock   | Paid-In   | Treasury   | Stock  | Noncontrolling |        |
|  | Deficit     | (Loss)       | Shares  | Amount  | Capital   | Shares     | Amount | Interest       |        |
| (In thousands)                           |             |              |         |         |           |            |        |                |        |
| <b>Balance</b>                           |             |              |         |         |           |            |        |                |        |
| <b>December 31, 2008</b>                 |             |              |         |         |           |            |        |                |        |
|  | \$ 104,710  | \$ (669,526) | \$ (29) | 121,589 | \$ 12,159 | \$ 763,323 | 929    | \$ (1,217)     | \$     |
| Net income (loss)                        | (8,555)     | (9,426)      |         |         |           |            |        |                | 871    |
| Impact of subsidiary equity transactions | 28,082      |              |         |         |           | 14,059     |        |                | 14,023 |
| Issuance of restricted stock, net        | 71          |              | 440     | 44      | (1,190)   | (929)      | 1,217  |                |        |
| Stock-based compensation expense         | 1,165       |              |         |         | 1,165     |            |        |                |        |
| Other comprehensive income               | 1           |              | 1       |         |           |            |        |                |        |
| <b>Balance</b>                           |             |              |         |         |           |            |        |                |        |
| <b>March 31, 2009</b>                    |             |              |         |         |           |            |        |                |        |
|  | \$ 125,474  | \$ (678,952) | \$ (28) | 122,029 | \$ 12,203 | \$ 777,357 | \$     | \$             | 14,894 |

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**SAFEGUARD SCIENTIFICS, INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**1. GENERAL**

The accompanying unaudited interim Consolidated Financial Statements of Safeguard Scientifics, Inc. (the Company) were prepared in accordance with accounting principles generally accepted in the United States of America and the interim financial statements rules and regulations of the SEC. In the opinion of management, these statements include all adjustments (consisting only of normal recurring adjustments) necessary for a fair presentation of the Consolidated Financial Statements. The interim operating results are not necessarily indicative of the results for a full year or for any interim period. Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been condensed or omitted pursuant to such rules and regulations relating to interim financial statements. The Consolidated Financial Statements included in this Form 10-Q should be read in conjunction with Management's Discussion and Analysis of Financial Condition and Results of Operations included elsewhere in this Form 10-Q and included together with the Company's Consolidated Financial Statements and Notes thereto included in the Company's 2008 Annual Report on Form 10-K.

**2. BASIS OF PRESENTATION**

The Consolidated Financial Statements include the accounts of the Company and its partner companies in which the Company owned more than 50% of the outstanding voting securities during the periods presented.

During the three months ended March 31, 2009, the Company's voting interest in Cellumen, Inc. (Cellumen) increased to 51.4%, on an as-converted basis, from 40.3%. Due to the substantive participating rights of the minority shareholders in the significant operating decisions of Cellumen, the Company continues to account for its holdings in Cellumen under the equity method. See Note 15 for additional information.

The Company's Consolidated Statements of Operations and Cash Flows for the three months ended March 31, 2009 and 2008 include Clariant, Inc. (Clariant) in continuing operations. During 2008, certain consolidated partner companies were sold and are reported in discontinued operations. See Note 3.

**3. DISCONTINUED OPERATIONS**

***Clariant Technology Business***

In March 2007, Clariant sold its technology business and related intellectual property to Carl Zeiss MicroImaging, Inc. (Zeiss) for an aggregate purchase price of \$12.5 million. The \$12.5 million consisted of \$11.0 million in cash and an additional \$1.5 million in contingent purchase price, subject to the satisfaction of certain post-closing conditions through March 2009. During March 2009, Clariant received correspondence from Zeiss which acknowledged the satisfaction of the post-closing conditions and the related \$1.5 million payment due. In April 2009, Clariant received \$1.5 million from Zeiss which was recorded in income from discontinued operations within the Consolidated Statement of Operations for the three months ended March 31, 2009.

***Acsis, Alliance Consulting and Laureate Pharma***

In May 2008, the Company consummated a transaction (the Bundle Sale) pursuant to which it sold all of its equity and debt interests in Acsis, Inc. (Acsis), Alliance Consulting Group Associates, Inc. (Alliance Consulting), Laureate Pharma, Inc. (Laureate Pharma), ProModel Corporation (ProModel) and Neuronix, Inc. (Neuronix) (collectively, the Bundle Companies).

Of the companies included in the Bundle Sale, Acsis, Alliance Consulting and Laureate Pharma were consolidated partner companies; Neuronix and ProModel were minority-owned partner companies. The Company has presented the results of operations of Acsis, Alliance Consulting and Laureate Pharma as discontinued operations for all periods presented.

In the first quarter of 2008, the Company recognized an impairment loss of \$3.6 million to write down the aggregate carrying value of the Bundle Companies to the total anticipated proceeds, less estimated costs to complete the Bundle Sale.



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The gross proceeds to the Company from the Bundle Sale were \$74.5 million, of which \$6.4 million was placed in escrow pending expiration of a claims period (see Note 16), plus amounts advanced to certain of the Bundle Companies during the time between the signing of the Bundle Sale agreement and its consummation. Guarantees of certain Bundle Company credit facilities by the Company of \$31.5 million were eliminated upon the closing of the Bundle Sale.

Results of all discontinued operations were as follows:

|  | <b>Three Months Ended March 31,</b> |             |
|--|-------------------------------------|-------------|
|  | <b>2009</b>                         | <b>2008</b> |
|  | <b>(In thousands)</b>               |             |
|  | <b>(unaudited)</b>                  |             |
| Revenue                                    | \$                                  | \$ 33,697   |
| Operating expenses                         |                                     | (36,190)    |
| Impairment of carrying value               |                                     | (3,634)     |
| Other                                      |                                     | (493)       |
| Loss from operations                       |                                     | (6,620)     |
| Gain (loss) on disposal, net of tax        | 1,500                               | (458)       |
| Income (loss) from discontinued operations | \$ 1,500                            | \$ (7,078)  |

**4. SUBSIDIARY EQUITY TRANSACTION**

On March 25, 2009, Clariant entered into a stock purchase agreement with Oak Investment Partners XII ( Oak ), pursuant to which Clariant agreed to sell up to an aggregate of 6.6 million shares of its Series A Convertible Preferred Stock in two or more tranches for aggregate consideration of up to \$50.0 million. Each preferred share is initially convertible, at any time, into four shares of Clariant s common stock, subject to adjustments. The initial closing of the Oak private placement occurred on March 26, 2009, at which time Clariant issued an aggregate of 3.8 million preferred shares for aggregate consideration of \$29.1 million. After paying closing fees and legal expenses, Clariant used the proceeds to repay in full and terminate its revolving credit agreement with a bank and repay a portion of the outstanding balance of its credit facility with the Company. Upon the consummation of the initial closing, the Company s ownership of issued and outstanding voting securities (on an as-converted basis) decreased to 50.2%.

Upon the second closing which is expected to occur in May 2009, Clariant will sell an additional 1.4 million preferred shares for approximately \$10.9 million. The second closing is contingent upon Clariant complying with all of the conditions for closing as set forth in the purchase agreement, including Clariant s obligation to obtain stockholder approval of the issuance of the preferred shares. Clariant expects to use a portion of the proceeds from the second closing to repay in full and terminate the subordinated revolving credit line provided by the Company and to use the remainder to support its working capital requirements.

The Company has accounted for the change in the Company s ownership interest in Clariant as an equity transaction. As a result, the Company recorded a \$14.1 million credit to additional paid-in capital in the first quarter of 2009 which represents the Company s increase in its investment in Clariant as a result of the Oak investment. In addition, the Company recorded an additional noncontrolling interest of \$14.0 million which represents the increase in noncontrolling interests as a result of the Oak investment. Upon the second closing, the Company s ownership of issued and outstanding voting securities, on an as-converted basis, is expected to decrease from 50.2% to 47.3% and the Company will deconsolidate its holdings in Clariant at the date.



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Marketable securities included the following:

|                                     | <b>March 31,<br/>2009</b> | <b>December 31,<br/>2008</b> |
|-------------------------------------|---------------------------|------------------------------|
|                                     | <b>(In thousands)</b>     |                              |
|                                     | <b>(unaudited)</b>        |                              |
| Held-to-maturity:                   |                           |                              |
| Commercial paper                    | \$ 1,296                  | \$ 1,551                     |
| Restricted U.S. Treasury securities |                           | 1,990                        |
| U.S. Treasury Bills                 | 1,992                     | 499                          |
| Government agency bonds             | 2,846                     | 351                          |
| Certificates of deposit             | 300                       | 12,300                       |
|                                     | <b>\$ 6,434</b>           | <b>\$ 16,691</b>             |

As of March 31, 2009, the contractual maturities of the marketable securities were less than one year.

Held-to-maturity securities are carried at amortized cost, which, due to the short-term maturity of these instruments, approximates fair value using quoted prices in active markets for identical assets or liabilities, defined as Level 1 inputs under SFAS No. 157.

**6. RECENT ACCOUNTING PRONOUNCEMENTS**

In April 2008, the Financial Accounting Standards Board ( FASB ) issued FASB Staff Position ( FSP ) FAS 142-3, Determination of the Useful Life of Intangible Assets. FSP FAS 142-3 amends the factors that should be considered in developing renewal or extension assumptions used to determine the useful life of a recognized intangible asset under Statement 142. FSP FAS 142-3 is effective for fiscal years beginning after December 15, 2008. The adoption of FSP FAS 142-3 did not have a material impact on the Company's Consolidated Financial Statements.

In November 2008, the FASB's Emerging Issues Task Force ( EITF ) reached a consensus on EITF Issue No. 08-6, Equity Method Accounting Considerations. EITF 08-6 continues to follow the accounting for the initial carrying value of equity method investments in APB Opinion No. 18, The Equity Method of Accounting for Investments in Common Stock, which is based on a cost accumulation model and generally excludes contingent consideration. EITF 08-6 also specifies that other-than-temporary impairment testing by the investor should be performed at the investment level and that a separate impairment assessment of the underlying assets is not required. An impairment charge by the investee should result in an adjustment of the investor's basis of the impaired asset for the investor's pro-rata share of such impairment. In addition, EITF 08-6 reached a consensus on how to account for an issuance of shares by an investee that reduces the investor's ownership share of the investee. An investor should account for such transactions as if it had sold a proportionate share of its investment with any gains or losses recorded through earnings. EITF 08-6 also addresses the accounting for a change in an investment from the equity method to the cost method after adoption of Statement 160. EITF 08-6 affirms the existing guidance in APB 18, which requires cessation of the equity method of accounting and application of SFAS No. 115, Accounting for Certain Investments in Debt and Equity Securities, or the cost method under APB 18 as appropriate. EITF 08-6 is effective for fiscal years beginning on or after December 15, 2008. The adoption of EITF 08-6 did not have a material impact on the Company's Consolidated Financial Statements.

In June 2008, the EITF ratified Issue No. 07-5, Determining Whether an Instrument (or Embedded Feature) Is Indexed to an Entity's Own Stock ( EITF 07-5 ). EITF 07-5 clarifies how to determine whether certain instruments or features were indexed to an entity's own stock. The consensus will replace EITF 01-6 as a critical component of the literature applied to evaluating financial instruments for debt or equity classification and embedded features for bifurcation as derivatives. EITF 07-5 is effective for financial statements issued for fiscal years beginning after December 15, 2008,

and interim periods within those fiscal years. The Company is currently analyzing the impact on the Company's Consolidated Financial Statements.



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**SAFEGUARD SCIENTIFICS, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

In May 2008, the FASB issued FSP No. APB 14-1, *Accounting for Convertible Debt Instruments That May Be Settled in Cash upon Conversion (Including Partial Cash Settlement)* ( FSP APB 14-1 ). FSP APB 14-1 requires the issuer of convertible debt instruments with cash settlement features to separately account for the liability and equity components of the instrument. The debt is recognized at the present value of its cash flows discounted using the issuer's nonconvertible debt borrowing rate. The equity component is recognized as the difference between the proceeds from the issuance of the note and the fair value of the liability. FSP APB 14-1 also requires an accretion of the resultant debt discount over the expected life of the debt. The adoption of FSP APB 14-1 did not have any impact on the Company's Consolidated Financial Statements because the convertible senior debentures issued by the Company do not include any cash settlement features within the scope of FSP APB 14-1.

In December 2007, the FASB issued SFAS No. 141 (revised 2007), *Business Combinations* ( SFAS 141(R) ). SFAS No. 141(R) significantly changes the accounting for business combinations. Under SFAS No. 141(R), an acquiring entity will be required to recognize all the assets acquired and liabilities assumed in a transaction at the acquisition-date at fair value with limited exceptions. SFAS No. 141(R) further changes the accounting treatment for certain specific items, including:

- Acquisition costs will be generally expensed as incurred;

- Noncontrolling interests (formerly known as minority interests see SFAS No. 160 discussion below) will be valued at fair value at the acquisition date;

- Acquired contingent liabilities will be recorded at fair value at the acquisition date and subsequently measured at either the higher of such amount or the amount determined under existing guidance for non-acquired contingencies;

- In-process research and development (IPR&D) will be recorded at fair value as an indefinite-lived intangible asset at the acquisition date;

- Restructuring costs associated with a business combination will be generally expensed subsequent to the acquisition date; and

Changes in deferred tax asset valuation allowances and income tax uncertainties after the acquisition date generally will affect income tax expense.

SFAS No. 141(R) includes a substantial number of new disclosure requirements. SFAS No. 141(R) applies prospectively to business combinations for which the acquisition date is on or after January 1, 2009.

In December 2007, the FASB issued SFAS No. 160, *Noncontrolling Interests in Consolidated Financial Statements* an amendment of ARB No. 51 ( SFAS No. 160 ). SFAS No. 160 establishes new accounting and reporting standards for the noncontrolling interest in a subsidiary and for the deconsolidation of a subsidiary. Specifically, this statement requires the recognition of noncontrolling interests (minority interests) as equity in the consolidated financial statements and separate from the parent's equity. The amount of net income attributable to noncontrolling interests will be included in consolidated net income on the face of the income statement. SFAS No. 160 clarifies that changes in a parent's ownership interest in a subsidiary that does not result in deconsolidation are treated as equity transactions if the parent retains its controlling financial interest. In addition, this statement requires that a parent recognize a gain or loss in net income when a subsidiary is deconsolidated. Such gain or loss will be measured using the fair value of the noncontrolling equity investment on the deconsolidation date. SFAS No. 160 also includes expanded disclosure requirements regarding the interests of the parent and its noncontrolling interest. SFAS No. 160 is effective for fiscal years beginning after November 15, 2008.

On January 1, 2009, the Company adopted the provisions of SFAS No. 160. As a result, the Company now reflects the portion of equity (net assets) of its consolidated partner companies not attributable, directly or indirectly, to the Company as a noncontrolling interest within equity, separate from the equity of the Company. Losses attributable to the noncontrolling interest that exceed its basis in the subsidiary's equity result in a deficit noncontrolling interest reflected in the Consolidated Balance Sheet. Revenue, expenses, gains, losses, net income or loss are reported in the Consolidated Statements of Operations at the consolidated amounts, which include the amounts attributable to the owners of the parent and noncontrolling interest.



**Table of Contents****SAFEGUARD SCIENTIFICS, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

All changes in the Company's ownership interest while it retains control of its consolidated partner companies are accounted for as equity transactions. Therefore, no gain or loss shall be recognized in the Consolidated Statement of Operations. In addition, the carrying amount of the noncontrolling interest shall be adjusted to reflect the change in ownership interest. Any difference between the fair value of the amounts received and the amounts by which the noncontrolling interest is adjusted is recognized by the Company as additional paid in capital. See Note 4.

**7. COMPREHENSIVE LOSS**

Comprehensive loss is the change in equity of a business enterprise from transactions and other events and circumstances from non-owner sources. Excluding net loss, the Company's sources of comprehensive loss are from foreign currency translation adjustments.

The following summarizes the components of comprehensive loss:

|   | <b>Three Months Ended March 31,</b> |             |
|---|-------------------------------------|-------------|
|   | <b>2009</b>                         | <b>2008</b> |
|   | <b>(In thousands)</b>               |             |
|   | <b>(unaudited)</b>                  |             |
| Net loss  | \$ (8,555)                          | \$ (19,243) |
| Other comprehensive income (loss), before taxes:                        |                                     |             |
| Foreign currency translation adjustments                                | 1                                   | 1           |
| Total comprehensive loss  | (8,554)                             | (19,242)    |
| Comprehensive (income) loss attributable to the noncontrolling interest | (871)                               | 389         |
| Comprehensive loss attributable to the Company                          | \$ (9,425)                          | \$ (18,853) |

**8. LONG-TERM DEBT AND CREDIT ARRANGEMENTS**

Consolidated long-term debt consisted of the following:

|   | <b>March 31,</b>      | <b>December 31,</b> |
|---|-----------------------|---------------------|
|   | <b>2009</b>           | <b>2008</b>         |
|   | <b>(In thousands)</b> |                     |
|   | <b>(unaudited)</b>    |                     |
| Consolidated partner company credit line borrowings (guaranteed by the Company)     | \$                    | \$ 9,000            |
| Consolidated partner company credit line borrowings (not guaranteed by the Company) | 5,887                 | 5,104               |
|   | 5,887                 | 14,104              |
| Capital lease obligations and other borrowings                                      | 1,759                 | 608                 |
|   | 7,646                 | 14,712              |
| Less current maturities   | (6,494)               | (14,367)            |
| Total long-term debt, less current portion  | \$ 1,152              | \$ 345              |



**Table of Contents****SAFEGUARD SCIENTIFICS, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

On February 6, 2009, the Company entered into a new loan agreement which provides the Company with a revolving credit facility in the maximum aggregate amount of \$50 million in the form of borrowings, guarantees and issuances of letters of credit (subject to a \$20 million sublimit). Actual availability under the credit facility will be based on the amount of cash maintained at the bank as well as the value of the Company's public and private partner company interests. This credit facility bears interest at the prime rate for outstanding borrowings, subject to an increase in certain circumstances. Other than for limited exceptions, the Company is required to maintain all of its depository and operating accounts and not less than 75% of its investment and securities accounts at the bank. The credit facility matures on December 31, 2010. In conjunction with the execution of the loan agreement, the Company is terminating its prior revolving credit facility.

Availability under the Company's new revolving credit facility at March 31, 2009 was \$50.0 million.

In connection with the sale of CompuCom Systems, Inc. (CompuCom) in 2004, the Company provided a letter of credit to the landlord of CompuCom's Dallas headquarters, which letter of credit will expire on March 19, 2019, in an amount equal to \$6.3 million. At March 31, 2009, the required cash collateral, pursuant to the Company's prior revolving credit facility, was \$6.3 million, which amount was included within Cash and cash equivalents on the Consolidated Balance Sheet as of that date.

On March 26, 2009, Clariant fully repaid the \$9.8 million outstanding balance under its \$12.0 million revolving credit agreement with a bank, using a portion of the proceeds from a private placement of its equity securities (see Note 4). The bank facility was terminated at such time. Clariant continues to maintain a \$2.3 million standby letter of credit with the bank which, beginning March 26, 2009, was fully supported by a restricted cash account in the same amount. The letter of credit is for the benefit of the landlord of Clariant's leased facility in Aliso Viejo, California.

On July 31, 2008, Clariant entered into a secured credit agreement with a finance company, which was amended on February 27, 2009 to extend its maturity date to January 31, 2010. The secured credit agreement is a revolving facility under which Clariant may borrow up to \$8.0 million, secured by Clariant's accounts receivable and related assets. The secured credit agreement's maturity date may be extended to January 31, 2011 upon the satisfaction of certain conditions, including (i) the absence of any continuing event of default and (ii) the extension or refinancing of the subordinated revolving credit line Safeguard provides to Clariant under terms which are satisfactory to the lender in its sole discretion.

During the three months ended March 31, 2009, our efforts continued in addressing the material weaknesses in our internal control over financial reporting. The steps we have undertaken in 2009 are discussed in Item 9A in our Annual Report on Form 10-K for the year ended December 31, 2008. We are in the process of evaluating the design and operating effectiveness of our internal control over financial reporting, which as a result of our remediation plan, include certain enhanced controls within the accounts receivable, revenue and billing processes.

Outstanding borrowings under the secured credit agreement were \$5.9 million at March 31, 2009. The amount which Clariant is entitled to borrow under the secured credit agreement at a particular time is based on the amount of Clariant's qualified accounts receivable and certain liquidity factors. Clariant had no additional availability as of March 31, 2009. As a result of the February 2009 amendment, borrowings under the secured credit agreement bear interest at annual rate equal to 30-day LIBOR (subject to a minimum annual rate of 2.50% at all times) plus an applicable margin of 6.0% during 2009 and 2010. Clariant is required to pay a commitment fee of 0.75% per year on the daily average of unused credit availability and a collateral monitoring fee of 0.40% per year on the daily average of outstanding borrowings.

The February 2009 amendment eliminated the previous minimum adjusted EBITDA covenant and replaced it with a covenant that requires Clariant to maintain a fixed charge coverage ratio as defined in the agreement on a cumulative annualized basis of 1.0 through June 30, 2009, 1.1 through September 30, 2009, and 1.2 through December 31, 2009. The February 2009 amendment also increased the capital expenditure limit to \$7.5 million in each fiscal year and increased the minimum level of excess liquidity as defined in the agreement, from \$2.0 million to \$3.0 million.

As of March 31, 2009, excluding the convertible senior debentures discussed in Note 9 below, the Company's debt matures as follows:

|                     | <b>Total</b><br><b>(In thousands)</b> |
|---------------------|---------------------------------------|
| Remainder of 2009   | \$ 440                                |
| 2010                | 6,560                                 |
| 2011                | 496                                   |
| 2012                | 150                                   |
| 2013 and thereafter |                                       |
|                     | \$ 7,646                              |

**Table of Contents****SAFEGUARD SCIENTIFICS, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****9. CONVERTIBLE SENIOR DEBENTURES**

In February 2004, the Company completed the sale of \$150 million of 2.625% convertible senior debentures with a stated maturity of March 15, 2024 (the 2024 Debentures). Interest on the 2024 Debentures is payable semi-annually. At the debentures holders' option, the 2024 Debentures are convertible into the Company's common stock through March 14, 2024, subject to certain conditions. The conversion rate of the debentures is \$7.2174 of principal amount per share. The closing price of the Company's common stock at March 31, 2009 was \$0.55. The 2024 Debentures holders have the right to require the Company to repurchase the 2024 Debentures on March 21, 2011, March 20, 2014 or March 20, 2019 at a repurchase price equal to 100% of their face amount, plus accrued and unpaid interest. The 2024 Debentures holders also have the right to require repurchase of the 2024 Debentures upon certain events, including sale of all or substantially all of our common stock or assets, liquidation, dissolution, a change in control or the delisting of the Company's common stock from the New York Stock Exchange if the Company were unable to obtain a listing for its common stock on another national or regional securities exchange. Subject to certain conditions, the Company may redeem all or some of the 2024 Debentures commencing March 20, 2009. The Company has repurchased \$64.0 million in face value of the 2024 Debentures. At March 31, 2009, the market value of the \$86.0 million outstanding 2024 Debentures was approximately \$63.6 million, based on quoted market prices as of such date.

As required by the terms of the 2024 Debentures, after completing the sale of CompuCom in October 2004, the Company escrowed \$16.7 million for interest payments through March 15, 2009 on the 2024 Debentures. Following the March 15, 2009 interest payment, the escrow account balance is \$0.0 million.

**10. STOCK-BASED COMPENSATION***Classification of Stock-Based Compensation Expense*

Stock-based compensation expense from continuing operations was recognized in the Consolidated Statements of Operations as follows:

|                                     | <b>Three Months Ended March 31,</b> |               |
|-------------------------------------|-------------------------------------|---------------|
|                                     | <b>2009</b>                         | <b>2008</b>   |
|                                     | <b>(In thousands)</b>               |               |
|                                     | <b>(unaudited)</b>                  |               |
| Cost of sales                       | \$ 33                               | \$ 36         |
| Selling, general and administrative | 1,132                               | 761           |
|                                     | <b>\$ 1,165</b>                     | <b>\$ 797</b> |

*The Company*

The fair value of the Company's stock-based awards to employees was estimated at the date of grant using the Black-Scholes option-pricing model. The risk-free rate was based on the U.S. Treasury yield curve in effect at the end of the quarter in which the grant occurred. The expected term of stock options granted was estimated using the historical exercise behavior of employees. Expected volatility was based on historical volatility measured using weekly price observations of the Company's common stock for a period equal to the stock option's expected term.

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**SAFEGUARD SCIENTIFICS, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

During the three months ended March 31, 2009, the Company issued 1.2 million restricted shares to employees. The restricted shares were issued in lieu of cash for a portion of the 2008 management incentive plan payment earned by certain senior employees. The restricted shares issued vest 25% on the first anniversary of grant and the remaining 75% thereafter in 24 equal monthly installments over the next two years.

The Company issued 109,000 and 36,000 deferred stock units during the three months ended March 31, 2009 and 2008, respectively, to non-employee directors for fees earned during the preceding quarter. For the three months ended March 31, 2009, all non-employee directors were required to defer at least 25% of directors' fees earned in the period and may have elected to defer up to 100% of directors' fees earned. For prior periods, certain directors elected to defer all or a portion of directors' fees earned. Deferred stock units issued to directors in lieu of directors' fees are 100% vested at the grant date; matching deferred stock units equal to 25% of directors' fees deferred vest one year following the grant date or, if earlier, upon reaching age 65. Deferred stock units are payable in stock on a one-for-one basis. Payments in respect of the deferred stock units are generally distributable following termination of employment or service, death or permanent disability.

Total compensation expense for deferred stock units and restricted stock was approximately \$0.1 million, and \$0.0 million for the three months ended March 31, 2009 and 2008, respectively.

The Company issued no stock option awards to employees during the three months ended March 31, 2009 and 2008, respectively.

At March 31, 2009, the Company had outstanding options that vest based on three different types of vesting schedules:

- 1) market-based;
- 2) performance-based; and
- 3) service-based.

Market-based awards entitle participants to vest in a number of options determined by achievement by the Company of certain target market capitalization increases (measured by reference to stock price increases on a specified number of outstanding shares) over an eight-year period. The requisite service periods for the market-based awards are based on the Company's estimate of the dates on which the market conditions will be met as determined using a Monte Carlo simulation model. Compensation expense is recognized over the requisite service periods using the straight-line method but is accelerated if market capitalization targets are achieved earlier than estimated. During the three months ended March 31, 2009, no options vested based on achievement of market capitalization targets. The Company recorded \$0.2 million and \$0.2 million of compensation expense related to these awards during the three months ended March 31, 2009 and 2008, respectively. Depending on the Company's stock performance, the maximum number of unvested shares at March 31, 2009 attainable under these grants was 7.8 million shares.

Performance-based awards entitle participants to vest in a number of options determined by achievement by the Company of target capital returns based on net cash proceeds received by the Company on the sale, merger or other exit transaction of certain identified partner companies over an eight-year period. Vesting may occur, if at all, once per year on the anniversary date of the grant. The requisite service periods for the performance-based awards are based on the Company's estimate of when the performance conditions will be met. Compensation expense is recognized for performance-based awards for which the performance condition is considered probable of achievement. Compensation expense is recognized over the requisite service periods using the straight-line method but is accelerated if capital return targets are achieved earlier than estimated. Compensation expense of \$0.1 was recognized related to these awards during the three months ended March 31, 2009. The maximum number of unvested shares at March 31, 2009 attainable under these grants was 2.0 million shares.

All other outstanding options are service-based awards that generally vest over four years after the date of grant and expire eight years after the date of grant. Compensation expense is recognized over the requisite service period using the straight-line method. The requisite service period for service-based awards is the period over which the award



vests. The Company recorded \$0.3 million and \$0.3 million of compensation expense related to these awards during the three months ended March 31, 2009 and 2008, respectively.

**Table of Contents****SAFEGUARD SCIENTIFICS, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****Consolidated Partner Company**

The fair value of the Company's consolidated partner company stock-based awards issued to employees during the three months ended March 31, 2009 and 2008 was estimated at the date of grant using the Black-Scholes option-pricing model. The risk-free rate was based on the U.S. Treasury yield curve in effect at the end of the quarter in which the grant occurred. The expected term of stock options granted was estimated using the historical exercise behavior of employees. Expected volatility for Clariant, the Company's publicly held consolidated partner company, was based on historical price volatility measured using weekly price observations of Clariant's common stock for a period equal to the stock option's expected term.

During the three months ended March 31, 2009, Clariant granted 1.1 million stock options. The options have four-year vesting terms and ten-year contractual terms. The fair value of these options at the date of grant was based on the following assumptions: a risk-free rate of 2.1%, an expected stock option term of five years, a dividend yield of 0.0% and expected five year volatility of 70%. Clariant estimates forfeitures of stock options using historical exercise behavior of its employees. For purposes of this estimate, Clariant identified two groups of employees and estimated the forfeiture rates for these groups to be 5% and 8% for the first three months of 2009. Clariant recorded \$0.6 million and \$0.3 million of stock-based compensation expense during the three months ended March 31, 2009 and 2008, respectively.

**11. INCOME TAXES**

The Company's consolidated income tax expense (benefit) was \$0.0 million for both the three months ended March 31, 2009 and 2008. The Company has recorded a valuation allowance to reduce its net deferred tax asset to an amount that is more likely than not to be realized in future years. Accordingly, the benefit of the net operating loss that would have been recognized in 2009 and 2008 was offset by a valuation allowance.

On January 1, 2007, the Company adopted FASB Interpretation No. 48, Accounting for Uncertainty in Income Taxes—an Interpretation of FASB Statement No. 109 (FIN 48). During the three months ended March 31, 2009, the Company had no material changes in uncertain tax positions.

**12. NET LOSS PER SHARE**

The calculations of net loss per share attributable to Safeguard Scientifics, Inc. common shareholders were:

|  | <b>Three Months Ended March 31,</b>         |             |
|--|---|-------------|
|  | <b>2009</b>                                 | <b>2008</b> |
|  | <b>(In thousands except per share data)</b> |             |
|  | <b>(unaudited)</b>                          |             |
| Basic and Diluted:                                       |   |             |
| Loss from continuing operations                          | \$ (10,321)                                 | \$ (11,778) |
| Income (loss) from discontinued operations               | 895   | (7,076)     |
| Net loss attributable to Safeguard Scientifics, Inc.     | \$ (9,426)                                  | \$ (18,854) |
| Average common shares outstanding                        | 121,645                                     | 122,996     |
| Net loss per share from continuing operations            | \$ (0.08)                                   | \$ (0.10)   |
| Net income (loss) per share from discontinued operations |   | (0.05)      |
| Net loss per share                                       | \$ (0.08)                                   | \$ (0.15)   |

Basic and diluted average common shares outstanding for purposes of computing net loss per share includes outstanding common shares and vested deferred stock units (DSUs).

**Table of Contents****SAFEGUARD SCIENTIFICS, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

If a consolidated or equity method partner company has dilutive stock options, unvested restricted stock, DSUs, warrants or securities outstanding, diluted net loss per share is computed by first deducting from net loss, the income attributable to the potential exercise of the dilutive securities of the company. This impact is shown as an adjustment to net loss for purposes of calculating diluted net loss per share.

The following potential shares of common stock and their effects on income were excluded from the diluted net loss per share calculation because their effect would be anti-dilutive:

At March 31, 2009 and 2008 options to purchase 20.0 million and 21.4 million shares of common stock, respectively, at prices ranging from \$0.65 to \$6.57 per share, were excluded from the calculations.

At March 31, 2009 and 2008, unvested restricted stock units and DSUs convertible into 1.4 million and 0.1 million shares of stock, respectively, were excluded from the calculations.

At March 31, 2009 and 2008, a total of 11.9 million and 17.9 million shares related to the Company's 2024 Debentures (see Note 9) representing the weighted average effect of assumed conversion of the 2024 Debentures were excluded from the calculations.

**13. PARENT COMPANY FINANCIAL INFORMATION**

Parent company financial information is provided to present the financial position and results of operations of the Company as if its consolidated partner company, Clariant, (see Note 2) was accounted for under the equity method of accounting for all periods presented during which the Company owned its interest in Clariant.

***Parent Company Balance Sheets***

|  | <b>March 31,<br/>2009</b> | <b>December 31,<br/>2008</b> |
|--|---------------------------|------------------------------|
|  | <b>(In thousands)</b>     |                              |
|  | <b>(unaudited)</b>        |                              |
| Assets:  |                           |                              |
| Cash and cash equivalents                              | \$ 84,346                 | \$ 73,213                    |
| Cash held in escrow – current                          | 6,433                     | 6,433                        |
| Marketable securities                                  | 6,434                     | 14,701                       |
| Restricted marketable securities                       |                           | 1,990                        |
| Other current assets                                   | 543                       | 356                          |
| Total current assets                                   | 97,756                    | 96,693                       |
| Ownership interests in and advances to companies       | 109,553                   | 105,955                      |
| Cash held in escrow – long-term                        | 476                       | 501                          |
| Other  | 1,228                     | 1,364                        |
| Total Assets   | \$ 209,013                | \$ 204,513                   |
| Liabilities and Shareholders' Equity:                  |                           |                              |
| Current liabilities                                    | \$ 6,992                  | \$ 8,173                     |
| Long-term liabilities                                  | 5,441                     | 5,630                        |
| Convertible senior debentures                          | 86,000                    | 86,000                       |
| Total Safeguard Scientifics, Inc. shareholders' equity | 110,580                   | 104,710                      |
| Total Liabilities and Shareholders' Equity             | \$ 209,013                | \$ 204,513                   |



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**SAFEGUARD SCIENTIFICS, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

***Parent Company Statements of Operations***

|  | <b>Three Months Ended March 31,</b> |             |
|--|-------------------------------------|-------------|
|  | <b>2009</b>                         | <b>2008</b> |
|  | <b>(In thousands)</b>               |             |
|  | <b>(unaudited)</b>                  |             |
| Operating expenses   | \$ (4,362)                          | \$ (5,297)  |
| Other income (loss), net                                     | (245)                               | 360         |
| Recovery related party                                       |                                     | 1           |
| Interest income  | 156                                 | 925         |
| Interest expense   | (735)                               | (1,055)     |
| Equity loss  | (5,135)                             | (6,712)     |
| Net loss from continuing operations before income taxes      | (10,321)                            | (11,778)    |
| Income tax benefit   |                                     |             |
| Equity income (loss) attributable to discontinued operations | 895                                 | (7,076)     |
| Net loss attributable to Safeguard Scientifics, Inc.         | \$ (9,426)                          | \$ (18,854) |

***Parent Company Statements of Cash Flows***

|  | <b>Three Months Ended March 31,</b> |             |
|--|-------------------------------------|-------------|
|  | <b>2009</b>                         | <b>2008</b> |
|  | <b>(In thousands)</b>               |             |
|  | <b>(unaudited)</b>                  |             |
| Net cash used in operating activities  | \$ (4,177)                          | \$ (3,069)  |
| <b>Cash Flows from Investing Activities</b>  |                                     |             |
| Advances to partner companies  | (6,050)                             | (14,571)    |
| Repayment of advances to partner companies   | 15,500                              |             |
| Acquisitions of ownership interests in partner companies and funds, net of cash acquired | (3,268)                             | (2,841)     |
| Repayment of note receivable-related party, net  |                                     | 1           |
| Increase in marketable securities  | (5,783)                             | (2,224)     |
| Decrease in marketable securities  | 14,050                              | 296         |
| Decrease in restricted cash  | 861                                 |             |
| Capital expenditures   |                                     | (6)         |
| Net cash provided by (used in) investing activities                                      | 15,310                              | (19,345)    |
| <b>Net Increase (Decrease) in Cash and Cash Equivalents</b>                              | 11,133                              | (22,414)    |
| Cash and Cash Equivalents at beginning of period   | 73,213                              | 94,685      |
| <b>Cash and Cash Equivalents at end of period</b>  | \$ 84,346                           | \$ 72,271   |

Parent Company cash and cash equivalents excludes marketable securities, which consist of longer-term securities.

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**SAFEGUARD SCIENTIFICS, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**14. OPERATING SEGMENTS**

As of March 31, 2009 the Company held an interest in one consolidated partner company, Clariant, and 16 non-consolidated partner companies. The Company's reportable operating segments are as follows: i) Clariant, its publicly traded consolidated partner company, ii) Life Sciences and iii) Technology.

The Life Sciences segment included the following partner companies as of March 31, 2009: Advanced BioHealing, Alverix, Avid Radiopharmaceuticals, Cellumen, Garnet BioTherapeutics, Molecular Biometrics, NuPathe, Rubicor and Tengion.

The Technology segment included the following partner companies as of March 31, 2009: Advantedge Healthcare Solutions, Authentium, Beyond.com, Bridgevine, GENBAND, Portico Systems and Swaptree.

Results of the Life Sciences and Technology segments reflect the equity income (loss) of their respective equity method partner companies, other income (loss) associated with cost method partner companies and the gains or losses on the sale of their respective partner companies.

Management evaluates the Clariant segment performance based on revenue, operating income (loss) and income (loss) before income taxes. Management evaluates the Life Sciences and Technology segments' performance based on net income (loss) which is based on the number of partner companies accounted for under the equity method, the Company's voting ownership percentage in these partner companies and the net results of operations of these partner companies and any impairment charges or gain (loss) on sale of partner companies.

Other Items include certain expenses which are not identifiable to the operations of the Company's operating business segments. Other Items primarily consist of general and administrative expenses related to corporate operations, including employee compensation, insurance and professional fees, including legal and finance, interest income, interest expense, other income (loss) and equity income (loss) related to private equity fund holdings. Other Items also include income taxes, which are reviewed by management independent of segment results.

The following tables reflect the Company's consolidated operating data by reportable segment. Segment results include the results of Clariant, the Company's consolidated partner company, impairment charges, gains or losses related to the disposition of partner companies (except those reported in discontinued operations) and the Company's share of income or losses for entities accounted for under the equity method. All significant intersegment activity has been eliminated in consolidation. Accordingly, segment results reported by the Company exclude the effect of transactions between the Company and its consolidated partner company.

Revenue is attributed to geographic areas based on where the services are performed or the customer's shipped to location. A majority of the Company's revenue is generated in the United States.

As of March 31, 2009 and December 31, 2008, the Company's assets were primarily located in the United States.

Segment assets in Other items included primarily cash, cash equivalents and marketable securities of \$90.8 million and \$87.9 million at March 31, 2009 and December 31, 2008, respectively.



**Table of Contents****SAFEGUARD SCIENTIFICS, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

The following represents segment data from continuing operations:

**Three Months Ended March 31, 2009**

|  | <b>Clarient</b> | <b>Life Sciences</b> | <b>Technology</b> | <b>Total Segments</b> | <b>Other Items</b> | <b>Total Continuing Operations</b> |
|--|-----------------|----------------------|-------------------|-----------------------|--------------------|------------------------------------|
|  |                 |                      |                   | <b>(In thousands)</b> |                    |                                    |
|  |                 |                      |                   | <b>(unaudited)</b>    |                    |                                    |
| Revenue  | \$ 22,447       | \$                   | \$                | \$ 22,447             | \$                 | \$ 22,447                          |
| Operating income (loss)  | 834             |                      |                   | 834                   | (4,362)            | (3,528)                            |
| Net income (loss) from continuing operations before income taxes | 644             | (3,424)              | (2,079)           | (4,859)               | (5,196)            | (10,055)                           |
| <b>Segment Assets:</b>   |                 |                      |                   |                       |                    |                                    |
| March 31, 2009   | 62,727          | 33,958               | 40,971            | 137,656               | 107,367            | 245,023                            |
| December 31, 2008  | 48,283          | 36,225               | 41,050            | 125,558               | 106,844            | 232,402                            |

**Three Months Ended March 31, 2008**

|   | <b>Clarient</b> | <b>Life Sciences</b> | <b>Technology</b> | <b>Total Segments</b> | <b>Other Items</b> | <b>Total Continuing Operations</b> |
|---|-----------------|----------------------|-------------------|-----------------------|--------------------|------------------------------------|
|   |                 |                      |                   | <b>(In thousands)</b> |                    |                                    |
|   |                 |                      |                   | <b>(unaudited)</b>    |                    |                                    |
| Revenue   | \$ 15,886       | \$                   | \$                | \$ 15,886             | \$                 | \$ 15,886                          |
| Operating loss  | (170)           |                      |                   | (170)                 | (5,297)            | (5,467)                            |
| Net loss from continuing operations before income taxes | (485)           | (4,386)              | (2,114)           | (6,985)               | (5,180)            | (12,165)                           |
| <b>Other Items</b>                                      |                 |                      |                   |                       |                    |                                    |

**Three Months Ended March 31, 2009**

|                      | <b>2009</b>           |         | <b>2008</b> |         |
|----------------------|-----------------------|---------|-------------|---------|
|                      | <b>(In thousands)</b> |         |             |         |
|                      | <b>(unaudited)</b>    |         |             |         |
| Corporate operations | \$                    | (5,196) | \$          | (5,180) |
| Income tax benefit   |                       |         |             |         |
|                      | \$                    | (5,196) | \$          | (5,180) |

**15. BUSINESS COMBINATIONS****Acquisitions by the Company 2009**

In March 2009, the Company increased its ownership interest in Bridgevine, Inc. ( Bridgevine ) to 24.4% from 21.1% for \$2.0 million in cash. The Company had previously acquired an interest in Bridgevine in August 2007 for \$8.0 million in cash. Bridgevine is an internet media company that enables online consumers to shop for special offers as well as compare and purchase digital services and products such as internet, phone, VoIP, TV, wireless, music, entertainment and more. The Company accounts for its holdings in Bridgevine under the equity method. The difference between the Company's cost and its interest in the underlying net assets of Bridgevine was allocated to

intangible assets and goodwill as reflected in the carrying value in Ownership interests in and advances to companies on the Consolidated Balance Sheet.

**Table of Contents****SAFEGUARD SCIENTIFICS, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

In February 2009, the Company provided additional funding to Cellumen as part of an up to \$2.5 million convertible note financing to be funded in five tranches. As part of this financing, the Company has agreed to provide Cellumen up to \$1.0 million (subject to certain conditions), \$0.3 million of which the Company funded at the initial closing. The Company previously acquired an interest in Cellumen in June 2007, paying \$6.0 million in cash for shares of Cellumen's Series B preferred stock. In conjunction with the convertible note financing, the Series B preferred stock conversion price was adjusted, and will receive further adjustments upon the closing of future tranches, increasing the economic and voting interest of the Series B preferred stock in Cellumen. After the funding of the initial tranche of convertible notes, the Company's voting interest in Cellumen increased to 51.4%, on an as-converted basis, from 40.3%. Due to the substantive participating rights of the minority shareholders in the significant operating decisions of Cellumen, the Company continues to account for its holdings in Cellumen under the equity method. Cellumen delivers proprietary services and products to support drug discovery and development.

In February 2009, the Company deployed an additional \$0.9 million in Molecular Biometrics, Inc. (Molecular Biometrics), maintaining a 37.8% ownership interest. The Company had previously acquired an interest in Molecular Biometrics in September and December 2008, for \$3.5 million in cash, including the conversion into equity interests of \$1.9 million previously advanced to the company. Molecular Biometrics is a metabolomics company developing novel clinical tools for applications in personalized medicine to more accurately characterize biologic function in health and disease. The Company accounts for its holdings in Molecular Biometrics under the equity method.

**16. COMMITMENTS AND CONTINGENCIES**

The Company and its partner companies are involved in various claims and legal actions arising in the ordinary course of business. While in the current opinion of the Company the ultimate disposition of these matters will not have a material adverse effect on the Company's consolidated financial position or results of operations, no assurance can be given as to the outcome of these actions, and one or more adverse rulings could have a material adverse effect on the Company's consolidated financial position and results of operations or that of its partner companies.

Not including the Laureate Lease Guaranty described below, the Company had outstanding guarantees of \$3.8 million at March 31, 2009.

The Company has committed capital of approximately \$6.8 million, including conditional commitments to provide non-consolidated partner companies with additional funding and commitments made to various private equity funds in prior years. These commitments will be funded over the next several years, including approximately \$6.5 million which is expected to be funded during the next 12 months.

Under certain circumstances, the Company may be required to return a portion or all the distributions it received as a general partner of certain private equity funds (the clawback). The maximum clawback the Company could be required to return due to its general partner interest is approximately \$3.6 million of which \$2.5 million was reflected in Accrued expenses and other current liabilities and \$1.1 million was reflected in Other long-term liabilities on the Consolidated Balance Sheet at March 31, 2009.

The Company's ownership in the funds which have potential clawback liabilities ranges from 19-30%. The clawback liability is joint and several; such that the Company may be required to fund the clawback for other general partners should they default. The funds have taken several steps to reduce the potential liabilities should other general partners default, including withholding all general partner distributions and placing them in escrow and adding rights of set-off among certain funds. The Company believes its potential liability due to the possibility of default by other general partners is remote.

Notwithstanding the closing of the Bundle Sale, the Company remains a guarantor of Laureate Pharma's Princeton, New Jersey office facility lease (the Laureate Lease Guaranty). Such guarantee may extend through the office lease expiration in 2016 under certain circumstances. However, the Company is entitled to indemnification in connection with the continuation of such guaranty. As of March 31, 2009, scheduled lease payments to be made by Laureate Pharma over the remaining lease term equaled \$8.6 million.



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**SAFEGUARD SCIENTIFICS, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

As described in Note 3, in connection with the Bundle Sale, an aggregate of \$6.4 million of the gross proceeds of the sale were placed in escrow pending the expiration of a predetermined notification period, subject to possible extension in the event of a claim against the escrowed amounts. On April 25, 2009, the purchaser in the Bundle Sale notified the Company of claims being asserted against the entire escrowed amounts. The Company does not believe that such claims are valid. The proceeds being held in escrow will remain there until the dispute over the claims have been settled or determined pursuant to legal process.

In October 2001, the Company entered into an agreement with Mr. Musser, its former Chairman and Chief Executive Officer, to provide for annual payments of \$0.7 million per year and certain health care and other benefits for life. The related current liability of \$0.8 million was included in Accrued expenses and the long-term portion of \$3.3 million was included in Other long-term liabilities on the Consolidated Balance Sheet at March 31, 2009.

**Table of Contents****Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations**  
**Cautionary Note Concerning Forward-Looking Statements**

This Quarterly Report on Form 10-Q contains forward-looking statements that are based on current expectations, estimates, forecasts and projections about Safeguard Scientifics, Inc. (Safeguard or we), the industries in which we operate and other matters, as well as management's beliefs and assumptions and other statements regarding matters that are not historical facts. These statements include, in particular, statements about our plans, strategies and prospects. For example, when we use words such as projects, expects, anticipates, intends, plans, believes, estimates, should, would, could, will, opportunity, potential or may, variations of such words or other phrases to convey uncertainty of future events or outcomes, we are making forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. Our forward-looking statements are subject to risks and uncertainties. Factors that could cause actual results to differ materially, include, among others, managing rapidly changing technologies, limited access to capital, competition, the ability to attract and retain qualified employees, the ability to execute our strategy, the uncertainty of the future performance of our partner companies, acquisitions and dispositions of companies, the inability to manage growth, compliance with government regulation and legal liabilities, additional financing requirements, labor disputes and the effect of economic conditions in the business sectors in which our partner companies operate, all of which are discussed in Item 1A. Risk Factors in Safeguard's Annual Report on Form 10-K and updated, as applicable, in Item 1A. Risk Factors below. Many of these factors are beyond our ability to predict or control. In addition, as a result of these and other factors, our past financial performance should not be relied on as an indication of future performance. All forward-looking statements attributable to us, or to persons acting on our behalf, are expressly qualified in their entirety by this cautionary statement. We undertake no obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events or otherwise, except as required by law. In light of these risks and uncertainties, the forward-looking events and circumstances discussed in this report might not occur.

**Business Overview**

Safeguard's charter is to build value in growth-stage technology and life sciences businesses. We provide capital as well as a range of strategic, operational and management resources to our partner companies. Safeguard participates in expansion financings, corporate spin-outs, management buy-outs, recapitalizations, industry consolidations and early-stage financings. Our vision is to be the preferred catalyst for creating great technology and life sciences companies.

We strive to create long-term value for our shareholders by helping our partner companies in their efforts to increase market penetration, grow revenue and improve cash flow in order to create long-term value. We concentrate on companies that operate in two categories:

*Life Sciences* including companies focused on molecular and point-of-care diagnostics, medical devices and regenerative medicine/specialty pharmaceuticals; and

*Technology* including companies focused on healthcare information technology, financial services information technology and new media and internet-based businesses.

**Principles of Accounting for Ownership Interests in Partner Companies**

We account for our interests in our partner companies and private equity funds using three methods: consolidation, equity or cost. The accounting method applied is generally determined by the degree of our influence over the entity, primarily determined by our voting interest in the entity.

*Consolidation Method.* We account for our partner companies in which we maintain a controlling financial interest, generally those in which we directly or indirectly own more than 50% of the outstanding voting securities, using the consolidation method of accounting. Upon consolidation of our partner companies, we reflect the portion of equity (net assets) in a subsidiary not attributable, directly or indirectly, to the Company as a noncontrolling interest in the Consolidated Balance Sheet. The noncontrolling interest is presented within equity, separately from the equity of the Company. Losses attributable to the Company and the noncontrolling interest may exceed their interest in the subsidiary's equity. As a result, the noncontrolling interest shall continue to be attributed its share of losses even if that attribution results in a deficit noncontrolling interest balance as of each balance sheet date. Revenue, expenses, gains,

losses, net income or loss are reported in the Consolidated Statements of Operations at the consolidated amounts, which include the amounts attributable to the Company's common shareholders and the noncontrolling interest.

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*Equity Method.* We account for partner companies whose results are not consolidated, but over whom we exercise significant influence, using the equity method of accounting. We also account for our interests in some private equity funds under the equity method of accounting, depending on our respective general and limited partner interests. Under the equity method of accounting, our share of the income or loss of the company is reflected in Equity Loss in the Consolidated Statements of Operations. We report our share of the income or loss of the equity method partner companies on a one quarter lag.

When the carrying value of our holding in an equity method partner company is reduced to zero, no further losses are recorded in our Consolidated Statements of Operations unless we have outstanding guarantee obligations or have committed additional funding to the equity method partner company. When the equity method partner company subsequently reports income, we will not record our share of such income until it equals the amount of our share of losses not previously recognized.

*Cost Method.* We account for partner companies which are not consolidated or accounted for under the equity method using the cost method of accounting. Under the cost method, our share of the income or losses of such partner companies is not included in our Consolidated Statements of Operations. However, the effect of the change in market value of cost method partner company holdings classified as trading securities is reflected in Other income (loss), net in the Consolidated Statements of Operations.

**Critical Accounting Policies and Estimates**

Accounting policies, methods and estimates are an integral part of the Consolidated Financial Statements prepared by management and are based upon management's current judgments. These judgments are normally based on knowledge and experience with regard to past and current events and assumptions about future events. Certain accounting policies, methods and estimates are particularly important because of their significance to the financial statements and because of the possibility that future events affecting them may differ from management's current judgments. While there are a number of accounting policies, methods and estimates affecting our financial statements, areas that are particularly significant include the following:

Revenue recognition;

Allowance for doubtful accounts and bad debt expense;

Impairment of long-lived assets;

Goodwill impairment;

Impairment of ownership interests in and advances to companies;

Income taxes;

Commitments and contingencies; and

Stock-based compensation.

***Revenue Recognition***

During the three months ended March 31, 2009 and 2008, our revenue from continuing operations was attributable to Clariant.

Revenue for Clariant's diagnostic testing and interpretive services is recognized at the time of completion of such services. Clariant's services are billed to various payors, including Medicare, health insurance companies and other directly billed healthcare institutions and patients. Clariant reports revenue from contracted payors, including certain health insurance companies and healthcare institutions, based on the contracted rate or, in certain instances, Clariant's estimate of such rate. For billings to Medicare, Clariant utilizes the published fee schedules, net of standard discounts commonly referred to as contractual allowances. Clariant reports revenue from non-contracted payors, including certain insurance companies and patients, based on the amount expected to be collected for services provided.



Adjustments resulting from actual collections compared to Clariant's estimates are recognized in the period realized.

**Table of Contents*****Allowance for Doubtful Accounts and Bad Debt Expense***

An allowance for doubtful accounts is recorded for estimated uncollectible amounts due from various payor groups such as Medicare and private health insurance companies. The process for estimating the allowance for doubtful accounts associated with Clariant's diagnostic services involves significant assumptions and judgments. Specifically, the allowance for doubtful accounts is adjusted periodically, based upon an evaluation of historical collection experience. Clariant also reviews the age of receivables by payor class to assess its allowance at each period end. The payment realization cycle for certain governmental and managed care payors can be lengthy; involving denial, appeal and adjudication processes, and is subject to periodic adjustments that may be significant. Accounts receivable are periodically written off when identified as uncollectible and deducted from the allowance for doubtful accounts after appropriate collection efforts have been exhausted. Additions to the allowance for doubtful accounts are charged to bad debt expense with Selling, general and administrative expense in the Consolidated Statements of Operations.

***Impairment of Long-Lived Assets***

We test long-lived assets, including property and equipment and amortizable intangible assets, for recoverability whenever events or changes in circumstances indicate that we may not be able to recover the asset's carrying amount. We evaluate the recoverability of an asset by comparing its carrying amount to the undiscounted cash flows expected to result from the use and eventual disposition of that asset. If the undiscounted cash flows are not sufficient to recover the carrying amount, we measure any impairment loss as the excess of the carrying amount of the asset over its fair value.

The carrying value of net property and equipment at March 31, 2009 was \$14.2 million.

***Impairment of Goodwill***

We conduct an annual review for impairment of goodwill as of December 1<sup>st</sup> and as otherwise required by circumstances or events. Additionally, on an interim basis, we assess the impairment of goodwill whenever events or changes in circumstances would more likely than not reduce the fair value of a reporting unit below its carrying amount. Factors that we consider important which could trigger an impairment review include significant underperformance relative to historical or expected future operating results, significant changes in the manner or use of the acquired assets or the strategy for the overall business, significant negative industry or economic trends, or a decline in a company's stock price for a sustained period.

We test for impairment at a reporting unit level (which for us is the same as an operating segment). If we determine that the fair value of a reporting unit is less than its carrying value, we assess whether goodwill of the reporting unit is impaired. To determine fair value, we use a number of valuation methods including quoted market prices, discounted cash flows, valuations of comparable public companies and valuations of acquisitions of comparable companies. Depending on the complexity of the valuation and the significance of the carrying value of the goodwill to the Consolidated Financial Statements, we may engage an outside valuation firm to assist us in determining fair value. As an overall check on the reasonableness of the fair values attributed to our reporting units, we will consider comparing the aggregate fair values for all reporting units with our average total market capitalization for a reasonable period of time.

The carrying value of goodwill at March 31, 2009 was \$12.7 million and relates entirely to our Clariant segment.

Our partner companies operate in industries which are rapidly evolving and extremely competitive. It is reasonably possible that our accounting estimates with respect to the ultimate recoverability of the carrying value of goodwill could change in the near term and that the effect of such changes on our Consolidated Financial Statements could be material. While we believe that the current recorded carrying value of our goodwill is not impaired, there can be no assurance that a significant write-down or write-off will not be required in the future.

**Table of Contents*****Impairment of Ownership Interests In and Advances to Companies***

On a periodic basis (but no less frequently than at the end of each quarter) we evaluate the carrying value of our equity and cost method partner companies for possible impairment based on achievement of business plan objectives and milestones, the financial condition and prospects of the company, market conditions, and other relevant factors. The business plan objectives and milestones we consider include, among others, those related to financial performance, such as achievement of planned financial results or completion of capital raising activities, and those that are not primarily financial in nature, such as hiring of key employees or the establishment of strategic relationships. We then determine whether there has been an other than temporary decline in the value of our ownership interest in the company. Impairment to be recognized is measured as the amount by which the carrying value of an asset exceeds its fair value.

The fair value of privately held partner companies is generally determined based on the value at which independent third parties have invested or have committed to invest in these companies or based on other valuation methods, including discounted cash flows, valuations of comparable public companies and valuations of acquisitions of comparable companies. The fair value of our ownership interests in private equity funds is generally determined based on the value of our pro rata portion of the funds' net assets and estimated future proceeds from sales of investments provided by the funds' managers.

The new carrying value of a partner company is not increased if circumstances suggest the value of the partner company has subsequently recovered.

Our partner companies operate in industries which are rapidly evolving and extremely competitive. It is reasonably possible that our accounting estimates with respect to the ultimate recoverability of the carrying value of ownership interests in and advances to companies could change in the near term and that the effect of such changes on our Consolidated Financial Statements could be material. While we believe that the current recorded carrying values of our equity and cost method companies are not impaired, there can be no assurance that our future results will confirm this assessment or that a significant write-down or write-off will not be required in the future.

Impairment charges related to equity method partner companies are included in Equity loss in the Consolidated Statements of Operations. Impairment charges related to cost method partner companies are included in Other income, net in the Consolidated Statements of Operations.

***Income Taxes***

We are required to estimate income taxes in each of the jurisdictions in which we operate. This process involves estimating our actual current tax exposure together with assessing temporary differences resulting from differing treatment of items for tax and accounting purposes. These differences result in deferred tax assets and liabilities, which are included within our Consolidated Balance Sheets. We must assess the likelihood that the deferred tax assets will be recovered from future taxable income and to the extent that we believe recovery is not likely, we must establish a valuation allowance. To the extent we establish a valuation allowance in a period; we must include an expense within the tax provision in the Consolidated Statements of Operations. We have recorded a valuation allowance to reduce our deferred tax assets to an amount that is more likely than not to be realized in future years. If we determine in the future that it is more likely than not that the net deferred tax assets would be realized, then the previously provided valuation allowance would be reversed.

***Commitments and Contingencies***

From time to time, we are a defendant or plaintiff in various legal actions which arise in the normal course of business. Additionally, we have received distributions as both a general partner and a limited partner from certain private equity funds. In certain circumstances, we may be required to return a portion or all the distributions we received as a general partner of a fund for a further distribution to such fund's limited partners (the "clawback"). We are also a guarantor of various third-party obligations and commitments and are subject to the possibility of various loss contingencies arising in the ordinary course of business (see Note 16). We are required to assess the likelihood of any adverse outcomes to these matters as well as potential ranges of probable losses. A determination of the amount of provision required for these commitments and contingencies, if any, which would be charged to earnings, is made after careful analysis of each matter. The provision may change in the future due to new developments or changes in circumstances. Changes in the provision could increase or decrease our earnings in the period the changes are made.



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***Stock-Based Compensation***

We measure all employee stock-based compensation awards using a fair value method and record such expense in our consolidated financial statements.

We estimate the grant date fair value of stock options using the Black-Scholes option-pricing model which requires the input of highly subjective assumptions. These assumptions include estimating the expected term of the award and the estimated volatility of our stock price over the expected term. Changes in these assumptions and in the estimated forfeitures of stock option awards can materially affect the amount of stock-based compensation recognized in the Consolidated Statements of Operations. The requisite service periods for market-based stock option awards are based on our estimate of the dates on which the market conditions will be met as determined using a Monte Carlo simulation model. Changes in the derived requisite service period or achievement of market capitalization targets earlier than estimated can materially affect the amount of stock-based compensation recognized in the Consolidated Statements of Operations. The requisite service periods for performance-based awards are based on our best estimate of when the performance conditions will be met. Compensation expense is recognized for performance-based awards for which the performance condition is considered probable of achievement. Changes in the requisite service period or the estimated probability of achievement of performance conditions can materially affect the amount of stock-based compensation recognized in the Consolidated Statements of Operations.

**Results of Operations**

We present Clariant, our publicly traded consolidated partner company, as a separate segment. The results of operations of our other partner companies are reported in our Life Sciences and Technology segments. The Life Sciences and Technology segments also include the gain or loss on the sale of respective partner companies, except for gains and losses included in discontinued operations.

Our management evaluates our Clariant segment performance based on revenue, operating income (loss) and income (loss) before income taxes. Our management evaluates our Life Sciences and Technology segments performance based on their equity income (loss) which is based on the number of respective partner companies accounted for under the equity method, the Company's voting ownership percentage in these partner companies and the net results of operations of these partner companies and Other income or loss associated with cost method partner companies.

Other Items include certain expenses, which are not identifiable to the operations of the Company's operating business segments. Other Items primarily consist of general and administrative expenses related to corporate operations, including employee compensation, insurance and professional fees, including legal and finance, interest income, interest expense, other income (loss) and equity income (loss) related to private equity holdings. Other Items also include income taxes, which are reviewed by management independent of segment results.

The following tables reflect our consolidated operating data by reportable segment. Segment results include the results of Clariant, our consolidated partner company, and our share of income or losses for entities accounted for under the equity method when applicable. Segment results also include impairment charges, gains or losses related to the disposition of partner companies, except for those reported in discontinued operations, and the mark-to-market of trading securities. All significant inter-segment activity has been eliminated in consolidation. Accordingly, segment results reported by us exclude the effect of transactions between us and our consolidated partner company.

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Our operating results including net income (loss) before income taxes by segment were as follows:

|   | <b>Three Months Ended March 31,</b> |             |
|---|-------------------------------------|-------------|
|   | <b>2009</b>                         | <b>2008</b> |
|   | <b>(In thousands)</b>               |             |
| Clariant  | \$ 644                              | \$ (485)    |
| Life Sciences   | (3,424)                             | (4,386)     |
| Technology  | (2,079)                             | (2,114)     |
| Total segments  | (4,859)                             | (6,985)     |
| Other items:  |                                     |             |
| Corporate operations                                      | (5,196)                             | (5,180)     |
| Income tax benefit  |                                     |             |
| Total other items   | (5,196)                             | (5,180)     |
| Net loss from continuing operations                       | (10,055)                            | (12,165)    |
| Income (loss) from discontinued operations, net of tax    | 1,500                               | (7,078)     |
| Net loss  | (8,555)                             | (19,243)    |
| Net (income) loss attributable to noncontrolling interest | (871)                               | 389         |
| Net loss attributable to the Company                      | \$ (9,426)                          | \$ (18,854) |

There is intense competition in the markets in which our partner companies operate, and we expect competition to intensify in the future. Additionally, the markets in which these companies operate are characterized by rapidly changing technology, evolving industry standards, frequent introduction of new products and services, shifting distribution channels, evolving government regulation, frequently changing intellectual property landscapes and changing customer demands. Their future success depends on each company's ability to execute its business plan and to adapt to its respective rapidly changing markets.

**Clariant**

The following table presents Clariant's results of operations:

|                                     | <b>Three Months Ended March 31,</b> |             |
|-------------------------------------|-------------------------------------|-------------|
|                                     | <b>2009</b>                         | <b>2008</b> |
|                                     | <b>(In thousands)</b>               |             |
| Revenue                             | \$ 22,447                           | \$ 15,886   |
| Operating expenses:                 |                                     |             |
| Cost of sales                       | 8,966                               | 7,397       |
| Selling, general and administrative | 12,647                              | 8,659       |
| Total operating expenses            | 21,613                              | 16,056      |
| Operating income (loss)             | 834                                 | (170)       |
| Interest, net                       | (190)                               | (315)       |

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|  |          |          |
|--|----------|----------|
| Income (loss) from continuing operations | 644      | (485)    |
| Income from discontinued operations      | 1,500    |          |
| Net income (loss)                        | \$ 2,144 | \$ (485) |

Clariant operates primarily in one business, the delivery of critical oncology testing services to community pathologists, biopharmaceutical companies and other researchers.

As of March 31, 2009, we owned a 50.2% voting interest in Clariant.

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*Three months ended March 31, 2009 versus the three months ended March 31, 2008*

*Revenue:* Revenue of \$22.4 million for the three months ended March 31, 2009 increased 41.3%, or \$6.6 million, from \$15.9 million in the prior year period. Clariant's increased revenue resulted from increased cancer diagnostic services volume, increased Medicare reimbursement rates and a favorable mix of higher value services performed in the current period. Clariant continues to expand its client base which has increased to approximately 950 active clients at March 31, 2009 from approximately 900 active clients at December 31, 2008.

During the first quarter of 2008, Clariant expanded the breadth of its cancer diagnostic testing services to include cancer markers for tumors of the colon, prostate and lung. Clariant expects to steadily increase its menu of cancer diagnostic services to include markers for additional tumor types and to deepen its market penetration for the diagnostic services that it currently provides. A number of recently published clinical findings have promoted the use of certain biomarkers to predict patient response to a class of colorectal cancer drugs that are focused on blocking the epidermal growth factor receptor ( EGFR ) signaling pathway. Clariant's tests such as K-ras (a newly emerging biomarker) to outline alterations in the EGFR pathway are therefore becoming a more recognized tool in the medical community for predicting an individual's response to drug therapies for colorectal cancers.

Clariant has also steadily increased the depth of its diagnostic services for certain cancer types that it has previously provided, including lymphoma/leukemia. Clariant's expanding capabilities in immunohistochemistry (IHC), flow cytometry, fluorescent in situ hybridization (FISH), and molecular/PCR, and its marketing of such capabilities, have enabled its revenue growth in the three months ended March 31, 2009 as compared to the prior year period. Clariant anticipates that its revenue will continue to increase as it further executes its operational strategy of expanding the breadth and depth of its cancer diagnostic services, and the means by which its services are marketed and delivered to its customers.

In July 2008, the Medicare rate increase for Technical CPT codes under the Physician Fee Schedule that retroactively took effect as of January 1, 2008 was extended eighteen months through December 31, 2009. Effective January 1, 2009, numerous other CPT codes under the Physician Fee Schedule and Clinical Fee Schedule for services Clariant performs generally increased through December 31, 2009.

*Cost of Sales.* Cost of sales for the three months ended March 31, 2009 was \$9.0 million compared to \$7.4 million in the prior year period, an increase of \$1.6 million, or 21.2%. The \$1.6 million increase was driven by the increase in volume as measured by the number of diagnostic tests performed; and was primarily related to additional laboratory personnel costs of \$0.4 million, increased laboratory supplies expense of \$0.6 million, increased cost of tests performed on Clariant's behalf by other laboratories of \$0.5 million and an increase in shipping expense of \$0.1 million.

Gross margin for the three months ended March 31, 2009 was 60.1% compared to 53.4% in the prior year period. The increase in gross margin was primarily driven by an overall increase in revenue, including higher value cancer diagnostic services. In addition, employee productivity continues to improve based on Clariant's metrics of specimens prepared and tested by month per full time equivalent (FTE) employee. Clariant also realized greater economies of scale in operations through its business growth as compared to the prior year.

Clariant anticipates that gross margins will improve as its testing volume increases. Clariant continues to improve the efficiency and effectiveness of its laboratory operations. Gross margins could be adversely affected, however, if the adjusted Medicare reimbursement rates (effective January 1, 2009) are decreased after December 31, 2009.

*Selling, General and Administrative.* Selling, general and administrative expenses for the three months ended March 31, 2009 were \$12.6 million, an increase of approximately \$4.0 million, or 46.1%, compared to \$8.7 million in the prior year period. The increase was primarily related to additional sales and marketing personnel costs of \$1.6 million (which included increased sales commission expense of \$0.7 million due to increased revenue), higher corporate development expenses of \$0.4 million, a \$0.3 million increase in stock-based compensation expense and a \$1.2 million increase in bad debt expense.

The increase in bad debt expense is primarily related to Clariant's increase in revenue as compared to the prior year and the impact on cash collections of delays in Clariant's internal billing and collection efforts. Bad debt expense was also impacted by higher loss experience in the second half of 2008 which increased the historical loss factor used in the bad debt calculation for the three months ended March 31, 2009. Clariant expects that bad debt expense as a



percentage of revenue in 2009 will be less as compared to 2008 as Clariant further staffs its in house billing and collection department, more effectively manages its billing and collection function and improves the quality of its billing and collection processes.

*Interest, Net.* Interest expense, net, was \$0.2 million and \$0.3 million for the three months ended March 31, 2009 and 2008, respectively. The decrease was due to lower outstanding borrowings under Clariant's third party financing facilities.

**Table of Contents****Life Sciences**

The following partner companies were included in Life Sciences during the three months ended March 31, 2009 and 2008:

| Partner Company                 | Safeguard Ownership as of March 31, |       | Accounting Method |
|---------------------------------|-------------------------------------|-------|-------------------|
|                                 | 2009                                | 2008  |                   |
| Advanced BioHealing, Inc.       | 28.3%                               | 28.3% | Equity Method     |
| Alverix, Inc.                   | 50.0%                               | 50.0% | Equity Method     |
| Avid Radiopharmaceuticals, Inc. | 13.9%                               | 14.2% | Cost Method       |
| Cellumen, Inc.                  | 51.4%                               | 40.3% | Equity Method (1) |
| Garnet BioTherapeutics, Inc.    | 31.1%                               | N/A   | Equity Method     |
| Molecular Biometrics, Inc.      | 37.8%                               | N/A   | Equity Method     |
| NuPathe, Inc.                   | 23.5%                               | 26.2% | Equity Method     |
| Rubicor Medical, Inc.           | 44.6%                               | 35.7% | Equity Method     |
| Tengion, Inc.                   | 4.5%                                | N/A   | Cost Method       |

(1) During the three months ended March 31, 2009, the Company's voting interest in Cellumen, Inc. increased to 51.4%, on an as-converted basis, from 40.3%. Due to the substantive participating rights of the minority shareholders in the significant operating decisions of Cellumen, the Company continues to account for its holdings in Cellumen under the equity method.

|             | Three Months Ended March 31, |            |
|-------------|------------------------------|------------|
|             | 2009                         | 2008       |
|             | (In thousands)               |            |
| Equity loss | \$ (3,424)                   | \$ (4,386) |

*Equity Loss.* Equity loss fluctuates with the number of Life Sciences partner companies accounted for under the equity method, our voting ownership percentage in these partner companies and the net results of operations of these partner companies. We recognize our share of losses to the extent we have cost basis in the equity partner company or we have outstanding commitments or guarantees. Certain amounts recorded to reflect our share of the income or losses of our partner companies accounted for under the equity method are based on estimates and on unaudited results of operations of those partner companies and may require adjustments in the future when audits of these entities are made final. We report our share of the results of our equity method partner companies on a one quarter lag basis. Equity loss for Life Sciences decreased \$1.0 million in the three months ended March 31, 2009 compared to the prior year period. The decrease in equity loss was primarily due to smaller losses incurred at certain partner companies.

**Table of Contents*****Technology***

The following partner companies were included in Technology during the three months ended March 31, 2009 and 2008:

| Partner Company                        | Safeguard Ownership as of March 31, |       | Accounting Method |
|--|-------------------------------------|-------|-------------------|
|  | 2009                                | 2008  |                   |
| Advantagede Healthcare Solutions, Inc. | 37.6%                               | 35.1% | Equity Method     |
| Authentium, Inc.                       | 20.0%                               | 19.9% | Equity Method (1) |
| Beyond.com, Inc.                       | 37.1%                               | 37.1% | Equity Method     |
| Bridgevine, Inc.                       | 24.4%                               | 20.8% | Equity Method     |
| Kadoo, Inc.(2)                         | 14.0%                               | 14.0% | Cost Method       |
| GENBAND, Inc.                          | 2.2%                                | 12.2% | Cost Method       |
| Portico Systems, Inc.                  | 46.0%                               | 46.8% | Equity Method     |
| Swaptree, Inc.                         | 29.3%                               | N/A   | Equity Method     |

- (1) During the third quarter of 2008, we increased our ownership interest in Authentium, Inc. to the 20.0% threshold at which we believe we exercise significant influence. Accordingly, we adopted the equity method of accounting for our holdings in Authentium. We have adjusted the financial statements for all prior periods presented to retrospectively apply the equity method of accounting for our holdings in Authentium since the initial date of acquisition in

April 2006

- (2) In the fourth quarter of 2008, we impaired the entire carrying value of Kadoo, Inc. which has since ceased operations.

|             | <b>Three Months Ended March 31,</b> |             |
|-------------|-------------------------------------|-------------|
|             | <b>2009</b>                         | <b>2008</b> |
|             | <b>(In thousands)</b>               |             |
| Equity loss | \$ (2,079)                          | \$ (2,114)  |

*Equity Loss.* Equity loss fluctuates with the number of Technology partner companies accounted for under the equity method, our voting ownership percentage in these partner companies and the net results of operations of these partner companies. We recognize our share of losses to the extent we have cost basis in the equity partner company or we have outstanding commitments or guarantees. Certain amounts recorded to reflect our share of the income or losses of our partner companies accounted for under the equity method are based on estimates and on unaudited results of operations of those partner companies and may require adjustments in the future when audits of these entities are made final. We report our share of the results of our equity method partner companies on a one quarter lag. Equity loss for Technology decreased \$0.1 million in the three months ended March 31, 2009 compared to the prior year period. The decrease was due to smaller losses incurred at certain partner companies.

**Table of Contents****Corporate Operations**

|                            | <b>Three Months Ended March 31,</b> |                   |
|----------------------------|-------------------------------------|-------------------|
|                            | <b>2009</b>                         | <b>2008</b>       |
|                            | <b>(In thousands)</b>               |                   |
| General and administrative | \$ (3,730)                          | \$ (4,733)        |
| Stock-based compensation   | (595)                               | (518)             |
| Depreciation               | (37)                                | (46)              |
| Interest income            | 156                                 | 925               |
| Interest expense           | (735)                               | (1,055)           |
| Other income (loss), net   | (245)                               | 361               |
| Equity loss                | (10)                                | (114)             |
|                            | <b>\$ (5,196)</b>                   | <b>\$ (5,180)</b> |

*Three months ended March 31, 2009 versus the three months ended March 31, 2008*

**General and Administrative Costs.** Our general and administrative expenses consist primarily of employee compensation, insurance, outside services such as legal, accounting and travel-related costs. General and administrative costs decreased \$1.0 million as compared to the prior year period. The decrease is primarily attributable to a \$0.2 million decrease in employee costs, \$0.4 million decrease in professional fees and \$0.1 million decrease in facility costs.

**Stock-Based Compensation.** Stock-based compensation consists primarily of expense related to stock option grants and grants of restricted stock and deferred stock units to our employees. The \$0.1 million increase relates to recent grants of performance-based stock options and restricted stock awards. Stock-based compensation expense related to corporate operations is included in selling, general and administrative in the Consolidated Statements of Operations.

**Interest Income.** Interest income includes all interest earned on available cash and marketable security balances. Interest income decreased \$0.8 million in the first quarter of 2009 compared to the prior year period due to a decrease in interest rates and a decrease in average invested cash balances.

**Interest Expense.** Interest expense is primarily related to our 2.625% convertible senior debentures with a stated maturity of 2024. Interest expense decreased \$0.3 million in the first quarter of 2009 as compared to the prior year period. The decline was attributable to the repurchase of \$43 million in face value of the 2024 Debentures in 2008.

**Other income (loss), net.** Other income (loss), net for the three months ended March 31, 2009 included an impairment charge related to a private equity fund of \$0.3 million. Other income (loss), net for the three months ended March 31, 2008 included a gain on sale of land of \$0.3 million.

**Equity loss.** Equity loss for both periods presented related to our private equity holdings accounted for under the equity method.

**Income Tax Expense**

Income tax expense (benefit) for the three months ended March 31, 2009 and 2008 was \$0 for both periods. We have recorded a valuation allowance to reduce our net deferred tax asset to an amount that is more likely than not to be realized in future years. Accordingly, the benefit of the net operating loss that would have been recognized in each period was offset by a valuation allowance.

**Table of Contents*****Discontinued Operations***

In March 2007, Clariant sold its technology business and related intellectual property to Carl Zeiss MicroImaging, Inc. ( Zeiss ) for an aggregate purchase price of \$12.5 million. (the ACIS Sale ) The \$12.5 million consisted of \$11.0 million in cash and an additional \$1.5 million in contingent purchase price, subject to the satisfaction of certain post-closing conditions through March 2009. During March 2009, Clariant received correspondence from Zeiss which acknowledged the satisfaction of the post-closing conditions and the related \$1.5 million payment due. In April 2009, Clariant received \$1.5 million from Zeiss which was recorded in income from discontinued operations within the Consolidated Statement of Operations for the three months ended March 31, 2009.

In May 2008, we consummated a transaction (the Bundle Sale ) pursuant to which we sold all of our equity and debt interests in Acsis, Inc. ( Acsis ), Alliance Consulting Group Associates, Inc. ( Alliance Consulting ), Laureate Pharma, Inc. ( Laureate Pharma ), ProModel Corporation ( ProModel ) and Neuronix, Inc. ( Neuronix ). Of the companies included in the Bundle Sale, Acsis, Alliance Consulting and Laureate Pharma were consolidated partner companies and are reported in discontinued operations for all periods presented. The loss from discontinued operations, net of tax in the first quarter of 2008 of \$7.1 million was primarily attributable to a \$3.6 million impairment loss related to the Bundle Sale and \$3.0 million in losses resulting from the first quarter operating results of Acsis, Alliance Consulting and Laureate Pharma.

***Liquidity and Capital Resources******Parent Company***

We fund our operations with cash on hand as well as proceeds from sales of and distributions from partner companies, private equity funds and marketable securities. In prior periods, we have also used sales of our equity and issuance of debt as sources of liquidity and may do so in the future. Our ability to generate liquidity from sales of partner companies, sales of marketable securities and from equity and debt issuances has been adversely affected from time to time by adverse circumstances in the U.S. capital markets and other factors.

As of March 31, 2009, at the parent company level, we had \$84.4 million of cash and cash equivalents and \$6.4 million of marketable securities for a total of \$90.8 million. In addition, we had \$6.9 million of cash held in escrow, including accrued interest, related to the Bundle Sale and the sale of Pacific Title and Art Studio. Clariant, our consolidated partner company, had cash and cash equivalents of \$4.7 million.

In connection with the Bundle Sale, an aggregate of \$6.4 million of the gross proceeds of the sale were placed in escrow pending the expiration of a predetermined notification period, subject to possible extension in the event of a claim against the escrowed amounts. On April 25, 2009, the purchaser in the Bundle Sale notified us of claims being asserted against the entire escrowed amounts. We do not believe that such claims are valid. The proceeds being held in escrow will remain there until the dispute over the claims have been settled or determined pursuant to legal process.

In February 2004, we completed the sale of the 2024 Debentures. At March 31, 2009, we had \$86.0 million in face value of the 2024 Debentures outstanding. Interest on the 2024 Debentures is payable semi-annually. At the holders option, the 2024 Debentures are convertible into our common stock before the close of business on March 14, 2024 subject to certain conditions. The conversion rate of the 2024 Debentures is \$7.2174 of principal amount per share. The closing price of our common stock on March 31, 2009 was \$0.55. The 2024 Debentures holders have the right to require repurchase of the 2024 Debentures on March 21, 2011, March 20, 2014 or March 20, 2019 at a repurchase price equal to 100% of their respective face amount, plus accrued and unpaid interest. The 2024 Debentures holders also have the right to require repurchase of the 2024 Debentures upon certain events, including sale of all or substantially all of our common stock or assets, liquidation, dissolution or a change in control. Subject to certain conditions, we have the right to redeem all or some of the 2024 Debentures. None of these conditions are satisfied as of today.

During 2008, we repurchased \$43.0 million in face value of the 2024 debentures for \$33.5 million in cash, including accrued interest. During 2006, we repurchased \$21.0 million in face value of the 2024 Debentures for \$16.4 million in cash, including accrued interest.





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On May 2, 2008, our Board of Directors authorized us, from time to time and depending on market conditions, to repurchase shares of our outstanding common stock, with up to an aggregate value of \$10.0 million, exclusive of fees and commissions. These repurchases, as well as any repurchases of 2024 Debentures, have and will be made in open market or privately negotiated transactions in compliance with the U.S. Securities and Exchange Commission and other applicable legal requirements. The manner, timing and amount of any purchases have and will be determined by us based upon an evaluation of market conditions, stock price and other factors. Our Board of Directors' authorizations regarding common stock and 2024 Debenture repurchases do not obligate us to acquire any particular amount of common stock or 2024 Debentures and may be modified or suspended at any time at our discretion. During the year ended December 31, 2008 we repurchased approximately 975 thousand shares of common stock at a cost of \$1.3 million.

On February 6, 2009, the Company entered into a new loan agreement which provides the Company with a revolving credit facility in the maximum aggregate amount of \$50 million in the form of borrowings, guarantees and issuances of letters of credit (subject to a \$20 million sublimit). Actual availability under the credit facility will be based on the amount of cash maintained at the bank as well as the value of the Company's public and private partner company interests. This credit facility bears interest at the prime rate for outstanding borrowings, subject to an increase in certain circumstances. Other than for limited exceptions, the Company is required to maintain all of its depository and operating accounts and not less than 75% of its investment and securities accounts at the bank. The credit facility matures on December 31, 2010. Availability under the Company's new revolving credit facility at March 31, 2009 was \$50.0 million.

In conjunction with the execution of the loan agreement, the Company is terminating its prior revolving credit facility. In connection with the sale of CompuCom Systems, Inc. ( CompuCom ) in 2004, the Company provided a letter of credit to the landlord of CompuCom's Dallas headquarters, which letter of credit will expire on March 19, 2019, in an amount equal to \$6.3 million. At March 31, 2009, the required cash collateral, pursuant to the Company's prior revolving credit facility, was \$6.3 million, which amount was included within Cash and cash equivalents on the Consolidated Balance Sheet as of that date.

We have committed capital of approximately \$6.8 million, including conditional commitments to provide non-consolidated partner companies with additional funding and commitments made to various private equity funds in prior years. These commitments will be funded over the next several years, including approximately \$6.5 million which is expected to be funded in the next 12 months. We may seek to further reduce our current ownership interests in, and our existing commitments to, the funds in which we hold interests.

The transactions we enter into in pursuit of our strategy could increase or decrease our liquidity at any point in time. As we seek to acquire interests in technology and life sciences companies or provide additional funding to existing partner companies, we may be required to expend our cash or incur debt, which will decrease our liquidity. Conversely, as we dispose of our interests in partner companies from time-to-time, we may receive proceeds from such sales which could increase our liquidity. From time-to-time, we are engaged in discussions concerning acquisitions and dispositions which, if consummated, could impact our liquidity, perhaps significantly.

In May 2001, we entered into a \$26.5 loan agreement with Warren V. Musser, our former Chairman and Chief Executive Officer. In December 2006, we restructured the obligation to reduce the amount outstanding to \$14.8 million, bearing an interest rate of 5.0% per annum. Cash payments, when received, are recognized as Recovery-related party in our Consolidated Statements of Operations. Since 2001 and through March 31, 2009 we received a total of \$16.3 million in cash payments on the loan. The carrying value of the loan at March 31, 2009 was zero.

We have received distributions as both a general partner and a limited partner from certain private equity funds. Under certain circumstances, we may be required to return a portion or all the distributions we received as a general partner of a fund for further distribution to such fund's limited partners (the clawback ). The maximum clawback we could be required to return for our general partner interest is \$3.6 million, of which \$2.5 million was reflected in accrued expenses and other current liabilities and \$1.1 million was reflected in Other long-term liabilities on the Consolidated Balance Sheet at March 31, 2009.

Our previous ownership in the general partners of the funds which have potential clawback liabilities ranges from 19-30%. The clawback liability is joint and several, such that we may be required to fund the clawback for other general partners should they default. The funds have taken several steps to reduce the potential liabilities should other general partners default, including withholding all general partner distributions and placing them in escrow and adding rights of set-off among certain funds. We believe our potential liability due to the possibility of default by other general partners is remote.

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For the reasons we presented above, we believe our cash and cash equivalents at March 31, 2009, availability under our revolving credit facility and other internal sources of cash flow will be sufficient to fund our cash requirements for at least the next 12 months, including commitments to our existing companies and funds, possible additional funding of existing partner companies and our general corporate requirements. Our acquisition of new partner company interests is always contingent upon our availability of cash to fund such deployments, and our timing of monetization events directly affects our availability of cash.

***Consolidated Partner Company***

On March 25, 2009 Clariant entered into a Stock Purchase Agreement with Oak Investment Partners XII ( Oak ) pursuant to which Clariant agreed to sell and issue to Oak, up to an aggregate of 6.6 million shares of its Series A Convertible Preferred Stock in two or more tranches for aggregate consideration of up to \$50.0 million. The initial closing occurred on March 26, 2009, at which time Clariant issued and sold 3.8 million preferred shares for proceeds of \$29.1 million. After paying closing fees and legal expenses, Clariant used the remaining proceeds to repay in full the outstanding balance of \$9.8 million on its revolving credit agreement, deposit \$2.3 million in a restricted cash account to support a standby letter of credit and repay us \$14.0 million of the outstanding balance on the subordinated revolving credit line we provide to Clariant (the Mezzanine Facility ). In connection with the Oak Purchase Agreement, on March 26, 2009, the Mezzanine Facility was amended to reduce the maximum principal amount from \$30.0 million to \$10.0 million.

On July 31, 2008, Clariant entered into a \$8.0 million secured credit agreement with a finance company which was amended and restated on February 27, 2009. The secured credit agreement expires on January 31, 2010. Actual availability under the facility is limited by Clariant's qualified accounts receivable and certain liquidity factors. Clariant reduced indebtedness to us under the Mezzanine Facility with a portion of the proceeds borrowed under the revolving credit facility.

In March 2007, we provided the Mezzanine Facility to Clariant. Under the Mezzanine Facility, we committed to provide Clariant access to up to \$12.0 million in working capital funding, which was reduced to \$6.0 million as a result of the ACIS Sale. On March 14, 2008, the Mezzanine Facility was extended through April 15, 2009, and increased from \$6.0 million to \$21.0 million. In connection with the extension and increase of the Mezzanine Facility, the Company received from Clariant five-year warrants to purchase shares of Clariant common stock with an exercise price of \$0.01 per share. The Company received 1.6 million of these warrants at the time of the extension of the Mezzanine Facility and the Company received an additional 1.7 million warrants through September 2008, based on the amount of borrowings remaining outstanding under the Mezzanine Facility at certain interim dates. On February 27, 2009 the Mezzanine Facility was further refinanced, renewed and expanded to \$30.0 million. In connection with such renewal, Clariant issued us fully vested five-year warrants to purchase 500,000 shares of Clariant common stock at an exercise price of \$1.376 (Clariant's 20-day trailing close price of its common stock as of February 6, 2009). The Mezzanine Facility as amended has a maturity date of April 1, 2010. Borrowings under the Mezzanine Facility bear interest at an annual rate of 14.0%.

Clariant expects a second closing to occur under the Oak Purchase Agreement on or about May 14, 2009, which will result in the issuance and sale of an additional 1.4 million preferred shares for proceeds of approximately \$10.9 million (the Second Oak Closing). Clariant expects to use a portion of the proceeds from the Second Oak Closing to repay in full and terminate the Mezzanine Facility and to use the remainder to support its working capital requirements.

Clariant believes that the collective funds to be made available in the Second Oak Closing, availability under its \$8.0 million secured credit agreement and the cash generated from its operations will be adequate to support its operations and growth through 2009 and into 2010. Nonetheless, Clariant can provide no assurance of such expectation. The level of cash collections by its billing and collection department during 2008 and the first quarter of 2009 have not increased at the same rate as its revenue has increased. Clariant relies on cash collections to support its general working capital needs, and therefore, if its cash collections in 2009 do not to keep pace with revenue growth, Clariant may require additional financing.



**Table of Contents****Analysis of Parent Company Cash Flows**

Cash flow activity for the Parent Company was as follows:

|   | <b>Three Months Ended March 31,</b> |             |
|---|-------------------------------------|-------------|
|   | <b>2009</b>                         | <b>2008</b> |
|   | <b>(In thousands)</b>               |             |
| Net cash used in operating activities               | \$ (4,177)                          | \$ (3,069)  |
| Net cash provided by (used in) investing activities | 15,310                              | (19,345)    |
| Net cash provided by financing activities           |                                     |             |
|   | \$ 11,133                           | \$ (22,414) |

**Cash Used In Operating Activities**

Cash used in operating activities increased \$1.1 million. The change was primarily related to working capital changes.

**Net Cash (Used in) Provided by Investing Activities**

Net cash provided by investing activities increased by \$34.7 million. The increase primarily related to a \$15.5 million increase in repayment of advances to partner companies, a decrease of \$8.5 million in advances to partner companies, a \$10.2 million net increase in cash from marketable securities and a \$0.8 million decrease in restricted cash.

**Consolidated Working Capital from Continuing Operations**

Consolidated working capital from continuing operations was \$109 million at March 31, 2009, an increase of \$20.6 million compared to December 31, 2008. The increase was primarily due to Clarient's sale of 3.8 million shares of preferred stock for \$29.1 million in cash, partially offset by Clarient's repayment of the outstanding balance of \$9.8 million on its revolving credit agreement.

**Analysis of Consolidated Company Cash Flows**

Cash flow activity was as follows:

|   | <b>Three Months Ended March 31,</b> |             |
|---|-------------------------------------|-------------|
|   | <b>2009</b>                         | <b>2008</b> |
|   | <b>(In thousands)</b>               |             |
| Net cash used in operating activities               | \$ (6,816)                          | \$ (6,308)  |
| Net cash provided by (used in) investing activities | 1,013                               | (8,409)     |
| Net cash provided by (used in) financing activities | 19,801                              | (7,093)     |
|   | \$ 13,998                           | \$ (21,810) |

**Net Cash Used In Operating Activities**

Cash used in operating activities increased \$0.5 million. The change was primarily related to working capital changes.

**Net Cash Provided by Investing Activities**

Net cash provided by investing activities increased by \$9.4 million. The increase is primarily related to a \$10.2 million net increase in cash from marketable securities, a \$2.1 million decrease in cash flows used in discontinued operations, partially offset by a \$2.0 million net increase in restricted cash, a \$0.4 million increase in cash used for acquisitions of ownership interests in partner companies and funds, net of cash acquired, a \$0.3 million increase in advances to partner companies and a \$0.2 million increase in capital expenditures.

**Table of Contents***Net Cash (Used In) Provided by Financing Activities*

Net cash provided by financing activities increased by \$26.9 million. The increase is primarily related to a \$27.9 million increase in proceeds from the issuance of subsidiary common stock offset by \$1.2 million net repayments on outstanding borrowings.

**Contractual Cash Obligations and Other Commercial Commitments**

The following table summarizes our contractual obligations and other commercial commitments related to continuing operations as of March 31, 2009 by period due or expiration of the commitment.

|   | <b>Payments Due by Period</b> |                                  |                          |                          |                           |
|---|-------------------------------|----------------------------------|--------------------------|--------------------------|---------------------------|
|   | <b>Total</b>                  | <b>Remainder<br/>of<br/>2009</b> | <b>2010 and<br/>2011</b> | <b>2012 and<br/>2013</b> | <b>Due after<br/>2013</b> |
|   | (In millions)                 |                                  |                          |                          |                           |
| <b>Contractual Cash Obligations:</b>      |                               |                                  |                          |                          |                           |
| Lines of credit                           | \$ 5.9                        | \$ 5.9                           | \$                       | \$                       | \$                        |
| Capital leases                            | 1.8                           | 0.4                              | 1.2                      | 0.2                      |                           |
| Convertible senior debentures(a)          | 86.0                          |                                  |                          |                          | 86.0                      |
| Operating leases                          | 14.4                          | 1.6                              | 4.5                      | 4.6                      | 3.7                       |
| Funding commitments(b)                    | 6.8                           | 6.4                              | 0.4                      |                          |                           |
| Potential clawback liabilities(c)         | 3.6                           | 2.5                              | 1.1                      |                          |                           |
| Other long-term obligations(d)            | 4.0                           | 0.6                              | 1.5                      | 1.5                      | 0.4                       |
| <b>Total Contractual Cash Obligations</b> | <b>\$ 122.5</b>               | <b>\$ 17.4</b>                   | <b>\$ 8.7</b>            | <b>\$ 6.3</b>            | <b>\$ 90.1</b>            |

|                           | <b>Amount of Commitment Expiration by Period</b> |                                  |                          |                          |                       |
|---------------------------|--|----------------------------------|--------------------------|--------------------------|-----------------------|
|                           | <b>Total</b>                                     | <b>Remainder<br/>of<br/>2009</b> | <b>2010 and<br/>2011</b> | <b>2012 and<br/>2013</b> | <b>After<br/>2013</b> |
|                           | (In millions)                                    |                                  |                          |                          |                       |
| <b>Other Commitments:</b> |  |                                  |                          |                          |                       |
| Letters of credit(e)      | \$ 8.6   | \$ 0.8                           | \$ 1.5                   | \$                       | \$ 6.3                |

(a) In February 2004, we completed the issuance of \$150.0 million in face value of the 2024 Debentures with a stated maturity of March 15, 2024. During 2008 and 2006, we repurchased \$43.0 million and \$21.0 million,

respectively, in face value of the 2024 Debentures. The 2024 Debenture holders have the right to require us to repurchase the 2024 Debentures on March 21, 2011, March 20, 2014 or March 20, 2019 at a repurchase price equal to 100% of their respective face amount, plus accrued and unpaid interest.

- (b) These amounts include funding commitments to private equity funds which have been included in the respective years based on estimated timing of capital calls provided to us by the funds management. Also included are \$5.9 million conditional commitments to provide non-consolidated partner companies with additional funding.
- (c) We have received distributions as both a general partner and a limited partner from certain

private equity funds. Under certain circumstances, we may be required to return a portion or all the distributions we received as a general partner of a fund for a further distribution to such fund's limited partners (the "clawback"). The maximum clawback we could be required to return is approximately \$3.6 million, of which \$2.5 million was reflected in accrued expenses and other current liabilities and \$1.1 million was reflected in other long-term liabilities on the Consolidated Balance Sheets.

- (d) Reflects the amount payable to our former Chairman and CEO under a contract.
- (e) Letters of credit include a \$6.3 million letter of credit provided to the landlord of CompuCom's Dallas headquarters lease in



connection with  
the sale of  
CompuCom in  
2004 and a  
\$2.3 million letter  
of credit issued  
by Clariant  
supporting its  
office lease.

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We have employment agreements with certain executive officers that provide for severance payments to the executive officer in the event the officer is terminated without cause or in the event the officer terminates his employment for good reason. The maximum aggregate exposure under the agreements was approximately \$8.0 million at March 31, 2009.

We are involved in various claims and legal actions arising in the ordinary course of business. In the opinion of management, the ultimate disposition of these matters will not have a material adverse effect on the consolidated financial position or results of operations.

***Recent Accounting Pronouncements***

See Note 6 to the Consolidated Financial Statements.

**Factors That May Affect Future Results**

You should carefully consider the information set forth below. The following risk factors describe situations in which our business, financial condition or results of operations could be materially harmed, and the value of our securities may decline. You should also refer to other information included or incorporated by reference in this report.

**Risks Related to our Business**

***Our business depends upon our ability to make good decisions regarding the deployment of capital into new or existing partner companies and, ultimately, the performance of our partner companies, which is uncertain.***

If we make poor decisions regarding the deployment of capital into new or existing partner companies, our business model will not succeed. Our success as a company ultimately depends on our ability to choose the right partner companies. If our partner companies do not succeed, the value of our assets could be significantly reduced and require substantial impairments or write-offs and our results of operations and the price of our common stock could decline. The risks relating to our partner companies include:

most of our partner companies have a history of operating losses or a limited operating history;

the intensifying competition affecting the products and services our partner companies offer could adversely affect their businesses, financial condition, results of operations and prospects for growth;

the inability to adapt to the rapidly changing marketplaces;

the inability to manage growth;

the need for additional capital to fund their operations, which we may not be able to fund or which may not be available from third parties on acceptable terms, if at all;

the inability to protect their proprietary rights and/or infringing on the proprietary rights of others;

the certain of our partner companies could face legal liabilities from claims made against them based upon their operations, products or work;

the impact of economic downturns on their operations, results and growth prospects;

the inability to attract and retain qualified personnel; and

the existence of government regulations and legal uncertainties may place financial burdens on the businesses of our partner companies.

These risks are discussed in greater detail under the caption **Risks Related to Our Partner Companies** below.

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***Our partner companies (and the nature of our interests in them) could vary widely from period to period.***

As part of our strategy, we continually assess the value to our shareholders of our interests in our partner companies. We also regularly evaluate alternative uses for our capital resources. As a result, depending on market conditions, growth prospects and other key factors, we may at any time:

change the partner companies on which we focus;

sell some or all of our interests in any of our partner companies; or

otherwise change the nature of our interests in our partner companies.

Therefore, the nature of our holdings could vary significantly from period to period.

Our consolidated financial results also may vary significantly based upon which partner companies are included in our financial statements. For example:

For the three months ended March 31, 2009 and year ended December 31, 2008, we consolidated the results of operations of Clariant in continuing operations.

***Our business model does not rely, or plan, upon the receipt of operating cash flows from our partner companies. Our partner companies currently provide us with no cash flow from their operations. We rely on cash on hand, liquidity events and our ability to generate cash from capital raising activities to finance our operations.***

We need capital to develop new partner company relationships and to fund the capital needs of our existing partner companies. We also need cash to service and repay our outstanding debt, finance our corporate overhead and meet our existing funding commitments. As a result, we have substantial cash requirements. Our partner companies currently provide us with no cash flow from their operations. To the extent our partner companies generate any cash from operations; they generally retain the funds to develop their own businesses. As a result, we must rely on cash on hand, liquidity events and new capital raising activities to meet our cash needs. If we are unable to find ways of monetizing our holdings or to raise additional capital on attractive terms, we may face liquidity issues that will require us to curtail our new business efforts, constrain our ability to execute our business strategy and limit our ability to provide financial support to our existing partner companies.

***Fluctuations in the price of the common stock of our publicly traded holdings may affect the price of our common stock.***

Fluctuations in the market prices of the common stock of our publicly traded holdings are likely to affect the price of our common stock. The market prices of our publicly traded holdings have been highly volatile and subject to fluctuations unrelated or disproportionate to operating performance. For example, the aggregate market value of our holdings in Clariant (Nasdaq: CLRT), our only public company holding, at March 31, 2009 was approximately \$104.6 million and at December 31, 2008 was approximately \$75.8 million.

***Intense competition from other acquirors of interests in companies could result in lower gains or possibly losses on our partner companies.***

We face intense competition from other capital providers as we acquire and develop interests in our partner companies. Some of our competitors have more experience identifying, acquiring and selling companies and have greater financial and management resources, brand name recognition or industry contacts than we have. Despite making most of our acquisitions at a stage when our partner companies are not publicly traded, we may still pay higher prices for those equity interests because of higher valuations of similar public companies and competition from other acquirors and capital providers, which could result in lower gains or possibly losses.

***We may be unable to obtain maximum value for our holdings or sell our holdings on a timely basis.***

We hold significant positions in our partner companies. Consequently, if we were to divest all or part of our holdings in a partner company, we may have to sell our interests at a relative discount to a price which may be received by a seller of a smaller portion. For partner companies with publicly traded stock, we may be unable to sell our holdings at then-quoted market prices. The trading volume and public float in the common stock of Clariant, our only publicly traded partner company, are small relative to our holdings. As a result, any significant open-market divestiture by us of our holdings in these partner companies, if possible at all, would likely have a material adverse effect on the market price of their common stock and on our proceeds from such a divestiture. Additionally, we may not be able to take our

partner companies public as a means of monetizing our position or creating shareholder value. Registration and other requirements under applicable securities laws may adversely affect our ability to dispose of our holdings on a timely basis.

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***Our success is dependent on our executive management.***

Our success is dependent on our executive management team's ability to execute our strategy. A loss of one or more of the members of our executive management team without adequate replacement could have a material adverse effect on us.

***Our business strategy may not be successful if valuations in the market sectors in which our partner companies participate decline.***

Our strategy involves creating value for our shareholders by helping our partner companies build value and, if appropriate, accessing the public and private capital markets. Therefore, our success is dependent on the value of our partner companies as determined by the public and private capital markets. Many factors, including reduced market interest, may cause the market value of our publicly traded partner companies to decline. If valuations in the market sectors in which our partner companies participate decline, their access to the public and private capital markets on terms acceptable to them may be limited.

***Our partner companies could make business decisions that are not in our best interests or with which we do not agree, which could impair the value of our holdings.***

Although we may seek a controlling equity interest and participation in the management of our partner companies, we may not be able to control the significant business decisions of our partner companies. We may have shared control or no control over some of our partner companies. In addition, although we currently own a controlling interest in some of our partner companies, we may not maintain this controlling interest. Acquisitions of interests in partner companies in which we share or have no control, and the dilution of our interests in or loss of control of partner companies, will involve additional risks that could cause the performance of our interests and our operating results to suffer, including:

- the management of a partner company having economic or business interests or objectives that are different than ours; and

- the partner companies not taking our advice with respect to the financial or operating difficulties they may encounter.

Our inability to control our partner companies also could prevent us from assisting them, financially or otherwise, or could prevent us from liquidating our interests in them at a time or at a price that is favorable to us. Additionally, our partner companies may not act in ways that are consistent with our business strategy. These factors could hamper our ability to maximize returns on our interests and cause us to recognize losses on our interests in these partner companies.

***We may have to buy, sell or retain assets when we would otherwise not wish to do so in order to avoid registration under the Investment Company Act.***

The Investment Company Act of 1940 regulates companies which are engaged primarily in the business of investing, reinvesting, owning, holding or trading in securities. Under the Investment Company Act, a company may be deemed to be an investment company if it owns investment securities with a value exceeding 40% of the value of its total assets (excluding government securities and cash items) on an unconsolidated basis, unless an exemption or safe harbor applies. We refer to this test as the 40% Test. Securities issued by companies other than consolidated partner companies are generally considered investment securities for purpose of the Investment Company Act; unless other circumstances exist which actively involve the company holding such interests in the management of the underlying company. We are a company that partners with growth-stage technology and life sciences companies to build value; we are not engaged primarily in the business of investing, reinvesting or trading in securities. We are in compliance with the 40% Test. Consequently, we do not believe that we are an investment company under the Investment Company Act.

We monitor our compliance with the 40% Test and seek to conduct our business activities to comply with this test. It is not feasible for us to be regulated as an investment company because the Investment Company Act rules are inconsistent with our strategy of actively helping our partner companies in their efforts to build value. In order to continue to comply with the 40% Test, we may need to take various actions which we would otherwise not pursue. For example, we may need to retain a controlling interest in a partner company that we no longer consider strategic, we may not be able to acquire an interest in a company unless we are able to obtain a controlling ownership interest in

the company, or we may be limited in the manner or timing in which we sell our interests in a partner company. Our ownership levels also may be affected if our partner companies are acquired by third parties or if our partner companies issue stock which dilutes our controlling ownership interest. The actions we may need to take to address these issues while maintaining compliance with the 40% Test could adversely affect our ability to create and realize value at our partner companies.

***Recent economic disruptions and downturns may have negative repercussions for the Company.***

Recent events in the United States and international capital markets, debt markets and economies generally may negatively impact the Company's ability to pursue certain of its tactical and strategic initiatives, such as: accessing additional public or private equity or debt financing for itself or for its partner companies and selling the Company's interests in its partner companies on terms acceptable to the Company and in time frames consistent with our expectations.

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***We have material weaknesses in our internal control over financial reporting and cannot provide assurance that additional material weaknesses will not be identified in the future. Our failure to effectively maintain our internal control over financial reporting could result in material misstatements in our financial statements which could require us to restate financial statements, cause us to fail to meet our reporting obligations, cause investors to lose confidence in our reported financial information and/or have a negative effect on our stock price.***

We have determined that we had deficiencies in our internal control over financial reporting as of December 31, 2008 that constituted material weaknesses as defined by the Public Company Accounting Oversight Board's Audit Standard No. 5. These material weaknesses are identified in Item 9A, Controls and Procedures within our Annual Report on Form 10-K for the year ended December 31, 2008.

We cannot assure that additional material weaknesses in our internal control over financial reporting will not be identified in the future. Any failure to maintain or implement required new or improved controls, or any difficulties we encounter in their implementation, could result in additional material weaknesses, or could result in material misstatements in our financial statements. These misstatements could result in a restatement of financial statements, cause us to fail to meet our reporting obligations and/or cause investors to lose confidence in our reported financial information, leading to a decline in our stock price.

***If we do not meet the New York Stock Exchange continued listing requirements, our common stock may be delisted.***

The New York Stock Exchange ( NYSE ) listing standards require us, among other things, to maintain an average closing price of at least \$1.00 per share of common stock during any consecutive 30-trading-day period. On November 4, 2008, we were notified by the NYSE that we were not in compliance with the NYSE listing standard relating to minimum average share price. We have notified the NYSE of our intent to cure the deficiency; and, if necessary, we will undertake a reverse split of our common stock in order to do so. Based on currently applicable NYSE rules, we must bring our share price and average share price back above \$1.00 on or before September 1, 2009, subject to possible extension, to regain compliance with the NYSE's price condition, or our common stock will be subject to suspension and delisting procedures. During the cure period and subject to compliance with NYSE's other continued listing standards; our common stock will continue to be listed on the NYSE.

A delisting of our common stock from the NYSE would negatively impact us because it would, unless we were able to obtain a listing for our common stock on another national or regional securities exchange, trigger a situation where the holders of our currently outstanding convertible debentures would have the right to cause us to redeem the convertible debentures held by such holders at face value. It is uncertain whether the Company would be able to make such redemption, based upon its available cash on hand, cash equivalents and other potential sources of funding. In addition, any delisting by the NYSE could or would also: (i) reduce the liquidity and market price of our common stock; (ii) reduce the number of investors willing to hold or acquire our common stock, which could negatively impact our ability to raise equity financing; (iii) limit our ability to use a registration statement to offer and sell freely tradable securities, thereby preventing us from accessing the public capital markets, and (iv) impair our ability to provide equity incentives to our employees.

***There could be negative effects if we do effect a reverse split of our Common Stock.***

If we undertake a reverse split of our stock in order to address the NYSE compliance issue described above, the immediate effect of a reverse stock split would be to reduce the number of shares of our outstanding common stock and to increase the trading price of our common stock. However, we cannot predict the specific effect of any reverse stock split upon the market price of our common stock. Based on the data we have reviewed it appears that sometimes a reverse stock split improves stock performance and sometimes it does not, and sometimes a reverse stock split improves overall market capitalization and sometimes it does not. We cannot assure you that the trading price of our common stock after the reverse stock split will rise in proportion to the reduction in the number of shares of our common stock outstanding as a result of the reverse stock split. Also, we cannot assure you that a reverse stock split would lead to a sustained increase in the trading price of our common stock. The trading price of our common stock may change due to a variety of factors, such as our operating results and other factors related to our business and general market conditions. We also cannot predict other possible negative effects of a reduction in the number of our common shares outstanding on the Company or on individual stockholders.





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**Risks Related to our Partner Companies**

***Most of our partner companies have a history of operating losses or limited operating history and may never be profitable.***

Most of our partner companies have a history of operating losses or limited operating history, have significant historical losses and may never be profitable. Many have incurred substantial costs to develop and market their products, have incurred net losses and cannot fund their cash needs from operations. We expect that the operating expenses of certain of our partner companies will increase substantially in the foreseeable future as they continue to develop products and services, increase sales and marketing efforts, and expand operations.

***Our partner companies face intense competition, which could adversely affect their business, financial condition, results of operations and prospects for growth.***

There is intense competition in the technology and life sciences marketplaces, and we expect competition to intensify in the future. Our business, financial condition, results of operations and prospects for growth will be materially adversely affected if our partner companies are not able to compete successfully. Many of the present and potential competitors may have greater financial, technical, marketing and other resources than those of our partner companies. This may place our partner companies at a disadvantage in responding to the offerings of their competitors, technological changes or changes in client requirements. Also, our partner companies may be at a competitive disadvantage because many of their competitors have greater name recognition, more extensive client bases and a broader range of product offerings. In addition, our partner companies may compete against one another.

***Our partner companies may fail if they do not adapt to the rapidly changing technology and life sciences marketplaces.***

If our partner companies fail to adapt to rapid changes in technology and customer and supplier demands, they may not become or remain profitable. There is no assurance that the products and services of our partner companies will achieve or maintain market penetration or commercial success, or that the businesses of our partner companies will be successful.

The technology and life sciences marketplaces are characterized by:

rapidly changing technology;

evolving industry standards;

frequently introducing new products and services;

shifting distribution channels;

evolving government regulation;

frequently changing intellectual property landscapes; and

changing customer demands.

Our future success will depend on our partner companies' ability to adapt to these rapidly evolving marketplaces. They may not be able to adequately or economically adapt their products and services, develop new products and services or establish and maintain effective distribution channels for their products and services. If our partner companies are unable to offer competitive products and services or maintain effective distribution channels, they will sell fewer products and services and forego potential revenue, possibly causing them to lose money. In addition, we and our partner companies may not be able to respond to the rapid technology changes in an economically efficient manner, and our partner companies may become or remain unprofitable.

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***Our partner companies may grow rapidly and may be unable to manage their growth.***

We expect some of our partner companies to grow rapidly. Rapid growth often places considerable operational, managerial and financial strain on a business. To successfully manage rapid growth, our partner companies must, among other things:

rapidly improve, upgrade and expand their business infrastructures;

scale up production operations;

develop appropriate financial reporting controls;

attract and maintain qualified personnel; and

maintain appropriate levels of liquidity.

If our partner companies are unable to manage their growth successfully, their ability to respond effectively to competition and to achieve or maintain profitability will be adversely affected.

***Based on our business model, some or all of our partner companies will need to raise additional capital to fund their operations at any given time. We may not be able to fund some or all of such amounts and such amounts may not be available from third parties on acceptable terms, if at all.***

We cannot be certain that our partner companies will be able to obtain additional financing on favorable terms, if at all. Because our resources and our ability to raise capital are limited, we may not be able to provide our partner companies with sufficient capital resources to enable them to reach a cash flow positive position. We also may fail to accurately project the capital needs of our partner companies for purposes of our cash flow planning. If our partner companies need to but are not able to raise capital from us or other outside sources, then they may need to cease or scale back operations. In such event, our interest in any such partner company will become less valuable.

***Recent economic disruptions and downturns may negatively affect our partner companies plans and their results of operations.***

Many of our partner companies are largely dependant upon outside sources of capital to fund their operations. Disruptions in the availability of capital from such sources will negatively affect the ability of such partner companies to pursue their business models and will force such companies to revise their growth and development plans accordingly. Any such changes will, in turn, affect the ability of the Company to realize the value of its capital deployments in such companies.

In addition, the downturn in the economy as well as possible governmental responses to such downturn and/or to specific situations in the economy could affect the business prospects of certain of our partner companies, including, but not limited to, in the following ways: weaknesses in the financial services industries; reduced business and/or consumer spending; and/or systematic changes in the ways the healthcare system operates in the United States.

***Our partner companies are subject to independent audits and the results of such independent audits could adversely impact our partner companies.***

As reported in its Form 10-K for the year ended December 31, 2008, Clariant's independent auditors have determined that there is substantial doubt about Clariant's ability to continue as a going concern. The going concern explanatory paragraph in Clariant's audit opinion could have a negative impact on:

Clariant's ability to extend, renew or refinance its bank credit facility or to secure additional debt or equity financing in order to fund anticipated working capital needs and capital expenditures and to execute its strategy;

Clariant's relationships with existing customers or potential new customers; and

Clariant's stock price.

If any of such events were to occur, the value of our holdings in Clariant could be adversely impacted.



**Table of Contents*****Some of our partner companies may be unable to protect their proprietary rights and may infringe on the proprietary rights of others.***

Our partner companies assert various forms of intellectual property protection. Intellectual property may constitute an important part of our partner companies' assets and competitive strengths. Federal law, most typically, copyright, patent, trademark and trade secret laws, generally protects intellectual property rights. Although we expect that our partner companies will take reasonable efforts to protect the rights to their intellectual property, the complexity of international trade secret, copyright, trademark and patent law, coupled with the limited resources of these partner companies and the demands of quick delivery of products and services to market, create a risk that their efforts will prove inadequate to prevent misappropriation of our partner companies' technology, or third parties may develop similar technology independently.

Some of our partner companies also license intellectual property from third parties and it is possible that they could become subject to infringement actions based upon their use of the intellectual property licensed from those third parties. Our partner companies generally obtain representations as to the origin and ownership of such licensed intellectual property; however, this may not adequately protect them. Any claims against our partner companies' proprietary rights, with or without merit, could subject our partner companies to costly litigation and the diversion of their technical and management personnel from other business concerns. If our partner companies incur costly litigation and their personnel are not effectively deployed, the expenses and losses incurred by our partner companies will increase and their profits, if any, will decrease.

Third parties have and may assert infringement or other intellectual property claims against our partner companies based on their patents or other intellectual property claims. Even though we believe our partner companies' products do not infringe any third-party's patents, they may have to pay substantial damages, possibly including treble damages, if it is ultimately determined that they do. They may have to obtain a license to sell their products if it is determined that their products infringe another person's intellectual property. Our partner companies might be prohibited from selling their products before they obtain a license, which, if available at all, may require them to pay substantial royalties. Even if infringement claims against our partner companies are without merit, defending these types of lawsuits takes significant time, may be expensive and may divert management attention from other business concerns.

***Certain of our partner companies could face legal liabilities from claims made against their operations, products or work.***

The manufacture and sale of certain of our partner companies' products entails an inherent risk of product liability. Certain of our partner companies maintain product liability insurance. Although none of our partner companies to date have experienced any material losses, there can be no assurance that they will be able to maintain or acquire adequate product liability insurance in the future and any product liability claim could have a material adverse effect on our partner companies' revenue and income. In addition, many of the engagements of our partner companies involve projects that are critical to the operation of their clients' businesses. If our partner companies fail to meet their contractual obligations, they could be subject to legal liability, which could adversely affect their business, operating results and financial condition. The provisions our partner companies typically include in their contracts, which are designed to limit their exposure to legal claims relating to their services and the applications they develop, may not protect our partner companies or may not be enforceable. Also, as consultants, some of our partner companies depend on their relationships with their clients and their reputation for high-quality services and integrity to retain and attract clients. As a result, claims made against our partner companies' work may damage their reputation, which in turn could impact their ability to compete for new work and negatively impact their revenue and profitability.

***Our partner companies' success depends on their ability to attract and retain qualified personnel.***

Our partner companies are dependent upon their ability to attract and retain senior management and key personnel, including trained technical and marketing personnel. Our partner companies also will need to continue to hire additional personnel as they expand. At present, none of our partner companies have employees represented by labor unions. Although our partner companies have not been the subject of a work stoppage, any future work stoppage could have a material adverse effect on their respective operations. A shortage in the availability of the requisite qualified personnel or work stoppage would limit the ability of our partner companies to grow, to increase sales of their existing products and services, and to launch new products and services.



**Table of Contents*****Government regulations and legal uncertainties may place financial burdens on the businesses of our partner companies.***

Failure to comply with applicable requirements of the FDA or comparable regulation in foreign countries can result in fines, recall or seizure of products, total or partial suspension of production, withdrawal of existing product approvals or clearances, refusal to approve or clear new applications or notices and criminal prosecution. Manufacturers of pharmaceuticals and medical diagnostic devices and operators of laboratory facilities are subject to strict federal and state regulation regarding validation and the quality of manufacturing and laboratory facilities. Failure to comply with these quality regulation systems requirements could result in civil or criminal penalties or enforcement proceedings, including the recall of a product or a cease distribution order. The enactment of any additional laws or regulations that affect healthcare insurance policy and reimbursement (including Medicare reimbursement) could negatively affect our partner companies. If Medicare or private payors change the rates at which our partner companies or their customers are reimbursed by insurance providers for their products, such changes could adversely impact our partner companies.

***Some of our partner companies are subject to significant environmental, health and safety regulation.***

Some of our partner companies are subject to licensing and regulation under federal, state and local laws and regulations relating to the protection of the environment and human health and safety, including laws and regulations relating to the handling, transportation and disposal of medical specimens, infectious and hazardous waste and radioactive materials, as well as to the safety and health of manufacturing and laboratory employees. In addition, the federal Occupational Safety and Health Administration have established extensive requirements relating to workplace safety.

**Item 3. Quantitative and Qualitative Disclosures About Market Risk**

We are exposed to equity price risks on the marketable portion of our securities. At March 31, 2009, these securities included our equity position in Clariant, our publicly traded partner company, which has experienced significant volatility in its stock price. Historically, we have not attempted to reduce or eliminate our market exposure on publicly traded securities. Based on closing market price at March 31, 2009, the fair market value of our holdings in Clariant was approximately \$104.6 million. A 20% decrease in Clariant's stock price as of that date would result in an approximate \$20.9 million decrease in the fair value of our holdings in Clariant.

In February 2004, we completed the issuance of \$150.0 million of our 2024 Debentures with a stated maturity of March 15, 2024. During 2008 and 2006, we repurchased \$43.0 million and \$21.0 million, respectively, in face value of the 2024 Debentures. Interest payments of approximately \$1.1 million each are due March and September of each year. The holders of these 2024 Debentures have the right to require repurchase of the 2024 Debentures on March 21, 2011, March 20, 2014 or March 20, 2019 at a repurchase price equal to 100% of their face amount plus accrued and unpaid interest.

|   | <b>Remainder<br/>of</b> |             |             |             | <b>After</b> | <b>Fair<br/>Value at<br/>March 31,<br/>2009</b> |
|---|-------------------------|-------------|-------------|-------------|--------------|---|
| <b>Liabilities</b>                        | <b>2009</b>             | <b>2010</b> | <b>2011</b> | <b>2011</b> |              |   |
| 2024 Debentures due by year (in millions) | \$                      | \$          | \$          | \$          | 86.0         | \$ 63.6   |
| Fixed interest rate                       | 2.625%                  | 2.625%      | 2.625%      | 2.625%      | 2.625%       | N/A   |
| Interest expense (in millions)            | \$ 1.7                  | \$ 2.3      | \$ 2.3      | \$ 2.3      | \$ 27.6      | N/A   |

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**Item 4. Controls and Procedures**

Our management, with the participation of our Chief Executive Officer and Chief Financial Officer, evaluated the effectiveness of our disclosure controls and procedures as of the end of the period covered by this report. Based on that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that, because of material weaknesses in internal control over financial reporting discussed in Management's Report on Internal Control Over Financial Reporting included in our Annual Report on Form 10-K for the year ended December 31, 2008 that were not remediated as of March 31, 2009, our disclosure controls and procedures were not effective to provide reasonable assurance that the information required to be disclosed by us in reports filed under the Securities Exchange Act of 1934 is (i) recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms and (ii) accumulated and communicated to our management, including the Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding disclosure. A controls system cannot provide absolute assurance that the objectives of the controls system are met, and no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within a company have been detected.

During the three months ended March 31, 2009, our efforts continued in addressing the material weaknesses in our internal control over financial reporting. The steps we have undertaken in 2009 are discussed in Item 9A in our Annual Report on Form 10-K for the year ended December 31, 2008. We are in the process of evaluating the design and operating effectiveness of our internal control over financial reporting, which as a result of our remediation plan, include certain enhanced controls within the accounts receivable, revenue and billing processes.

In light of our unremediated material weaknesses, we performed additional post-closing procedures and analyses in order to prepare the Consolidated Financial Statements included in this report. As a result of these procedures, we believe our Consolidated Financial Statements included in this report present fairly, in all material respects, our financial condition, results of operations and cash flows for the periods presented.

No change in our internal control over financial reporting occurred during our most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting. Our business strategy involves the acquisition of new businesses on an on-going basis, most of which are young, growing companies. Typically, these companies have not historically had all of the controls and procedures they would need to comply with the requirements of the Securities Exchange Act of 1934 and the rules promulgated there under. These companies also frequently develop new products and services. Following an acquisition, or the launch of a new product or service, we work with the company's management to implement all necessary controls and procedures.

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**PART II OTHER INFORMATION**

**Item 1A. Risk Factors**

Except as set forth below, there have been no material changes in our risk factors from the information set forth above under the heading Factors That May Affect Future Results and in our Annual Report on Form 10-K for the year ended December 31, 2008.

***Fluctuations in the price of the common stock of our publicly traded holdings may affect the price of our common stock.***

Fluctuations in the market prices of the common stock of our publicly traded holdings are likely to affect the price of our common stock. The market prices of our publicly traded holdings have been highly volatile and subject to fluctuations unrelated or disproportionate to operating performance. For example, the aggregate market value of our holdings in Clariant (Nasdaq: CLRT) at March 31, 2009 was approximately \$104.6 million, and at December 31, 2008 was approximately \$75.8 million.

In addition to the other information set forth in this report, you should carefully consider the factors discussed in Part I, Item 1A. Risk Factors in our Annual Report on Form 10-K for the year ended December 31, 2008, which could materially affect our business, financial condition or future results. The risks described in this report and in our Annual Report on Form 10-K are not the only risks facing our Company. Additional risks and uncertainties not currently known to us or that we currently deem to be immaterial also may materially adversely affect our business, financial condition and/or operating results.

***Our partner companies (and the nature of our interests in them) could vary widely from period to period.***

As part of our strategy, we continually assess the value to our shareholders of our interests in our partner companies. We also regularly evaluate alternative uses for our capital resources. As a result, depending on market conditions, growth prospects and other key factors, we may at any time:

- change the partner companies on which we focus;
- sell some or all of our interests in any of our partner companies; or
- otherwise change the nature of our interests in our partner companies.

Therefore, the nature of our holdings could vary significantly from period to period. Our consolidated financial results also may vary significantly based upon which partner companies are included in our financial statements.



**Table of Contents****Item 6. Exhibits**

## (a) Exhibits.

The following is a list of exhibits required by Item 601 of Regulation S-K filed as part of this Report. For exhibits that previously have been filed, the Registrant incorporates those exhibits herein by reference. The exhibit table below includes the Form Type and Filing Date of the previous filing and the location of the exhibit in the previous filing which is being incorporated by reference herein. Documents which are incorporated by reference to filings by parties other than the Registrant are identified in a footnote to this table.

| Exhibit Number | Description   | Incorporated Filing Reference |                         |
|----------------|---|-------------------------------|-------------------------|
|                |   | Form Type & Filing Date       | Original Exhibit Number |
| 10.1*          | Safeguard Scientifics, Inc. Executive Deferred Compensation Plan (amended and restated as of January 1, 2009)   | Form 10-K<br>3/19/09          | 10.4                    |
| 10.2           | Loan and Security Agreement dated as of February 6, 2009, by and among Silicon Valley Bank, Safeguard Scientifics, Inc., Safeguard Delaware, Inc. and Safeguard Scientifics (Delaware), Inc.                | Form 8-K<br>2/11/09           | 10.1                    |
| 10.3           | Fourth Amendment to Amended and Restated Loan Agreement, dated as of January 27, 2009, by and between Comerica Bank and Clariant, Inc.  | (1)                           | 10.2                    |
| 10.4           | Fifth Amendment to Amended and Restated Loan Agreement dated February 27, 2009, by and between Clariant, Inc. and Comerica Bank   | (2)                           | 10.2                    |
| 10.5           | Second Amended and Restated Senior Subordinated Revolving Credit Agreement dated February 27, 2009 by and between Safeguard Delaware, Inc. and Clariant, Inc.   | (2)                           | 10.3                    |
| 10.6           | Amended and Restated Registration Rights Agreement dated February 27, 2009 by and among Safeguard Delaware, Inc., Safeguard Scientifics, Inc., Safeguard Scientifics (Delaware), Inc. and Clariant, Inc.    | (2)                           | 10.4                    |
| 10.7           | Amendment to Securities Purchase Agreement dated March 26, 2009, by and between Clariant, Inc. and Safeguard Delaware, Inc. and its affiliates  | (3)                           | 10.4                    |
| 10.8           | First Amendment and Consent to Second Amended and Restated Senior Subordinated Revolving Credit Agreement dated March 26, 2009 by and between Safeguard Delaware, Inc. and Clariant, Inc.                   | (3)                           | 10.5                    |
| 10.9           | Stockholders Agreement dated March 26, 2009 by and among Safeguard Delaware, Inc., Safeguard Scientifics, Inc., Safeguard Scientifics (Delaware), Inc. and Oak Investment Partners XII, Limited Partnership | (3)                           | 10.6                    |
| 31.1           | Certification of Peter J. Boni pursuant to Rules 13a-15(e) and 15d-15(e) of the Securities Exchange Act of 1934   |                               |                         |
| 31.2           | Certification of Stephen T. Zarrilli pursuant to Rules 13a-15(e) and 15d-15(e) of the Securities Exchange Act of 1934   |                               |                         |
| 32.1           |   |                               |                         |

Certification of Peter J. Boni pursuant to 18 U.S.C. Section 1350, as Adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

32.2 Certification of Stephen T. Zarrilli pursuant to 18 U.S.C. Section 1350, as Adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

Filed herewith.

- \* Management contracts or compensatory plans, contracts or arrangements in which directors and/or executive officers of the Registrant may participate.
- (1) Incorporated by reference to the Current Report on Form 8-K filed on February 2, 2009 by Clariant, Inc. (SEC File No. 000-22677).
- (2) Incorporated by reference to the Current Report on Form 8-K filed on March 2, 2009 by Clariant, Inc. (SEC File No. 000-22677).
- (3) Incorporated by reference to the Current Report on Form 8-K filed on March 27, 2009 by Clariant, Inc. (SEC File No. 000-22677).



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**SIGNATURES**

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

SAFEGUARD SCIENTIFICS, INC.

Date: May 11, 2009

PETER J. BONI  
Peter J. Boni  
*President and Chief Executive Officer*

Date: May 11, 2009

STEPHEN T. ZARRILLI  
Stephen T. Zarrilli  
*Senior Vice President and Chief Financial Officer*

Table of Contents**EXHIBIT INDEX**

| Exhibit<br>Number | Description   | Incorporated Filing<br>Reference |                               |
|-------------------|---|----------------------------------|-------------------------------|
|                   |   | Form Type<br>&<br>Filing Date    | Original<br>Exhibit<br>Number |
| 10.1*             | Safeguard Scientifics, Inc. Executive Deferred Compensation Plan (amended and restated as of January 1, 2009)   | Form 10-K<br>3/19/09             | 10.4                          |
| 10.2              | Loan and Security Agreement dated as of February 6, 2009, by and among Silicon Valley Bank, Safeguard Scientifics, Inc., Safeguard Delaware, Inc. and Safeguard Scientifics (Delaware), Inc.                | Form 8-K<br>2/11/09              | 10.1                          |
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| 10.4              | Fifth Amendment to Amended and Restated Loan Agreement dated February 27, 2009, by and between Clariant, Inc. and Comerica Bank   | (2)                              | 10.2                          |
| 10.5              | Second Amended and Restated Senior Subordinated Revolving Credit Agreement dated February 27, 2009 by and between Safeguard Delaware, Inc. and Clariant, Inc.   | (2)                              | 10.3                          |
| 10.6              | Amended and Restated Registration Rights Agreement dated February 27, 2009 by and among Safeguard Delaware, Inc., Safeguard Scientifics, Inc., Safeguard Scientifics (Delaware), Inc. and Clariant, Inc.    | (2)                              | 10.4                          |
| 10.7              | Amendment to Securities Purchase Agreement dated March 26, 2009, by and between Clariant, Inc. and Safeguard Delaware, Inc. and its affiliates  | (3)                              | 10.4                          |
| 10.8              | First Amendment and Consent to Second Amended and Restated Senior Subordinated Revolving Credit Agreement dated March 26, 2009 by and between Safeguard Delaware, Inc. and Clariant, Inc.                   | (3)                              | 10.5                          |
| 10.9              | Stockholders Agreement dated March 26, 2009 by and among Safeguard Delaware, Inc., Safeguard Scientifics, Inc., Safeguard Scientifics (Delaware), Inc. and Oak Investment Partners XII, Limited Partnership | (3)                              | 10.6                          |
| 31.1              | Certification of Peter J. Boni pursuant to Rules 13a-15(e) and 15d-15(e) of the Securities Exchange Act of 1934   |                                  |                               |
| 31.2              | Certification of Stephen T. Zarrilli pursuant to Rules 13a-15(e) and 15d-15(e) of the Securities Exchange Act of 1934   |                                  |                               |
| 32.1              | Certification of Peter J. Boni pursuant to 18 U.S.C. Section 1350, as Adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.  |                                  |                               |
| 32.2              | Certification of Stephen T. Zarrilli pursuant to 18 U.S.C. Section 1350, as Adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.  |                                  |                               |

Filed herewith.

- \* Management contracts or compensatory plans, contracts or arrangements in which directors and/or executive officers of the Registrant may participate.
- (1) Incorporated by reference to the Current Report on Form 8-K filed on February 2, 2009 by Clariant, Inc. (SEC File No. 000-22677).
- (2) Incorporated by reference to the Current Report on Form 8-K filed on March 2, 2009 by Clariant, Inc. (SEC File No. 000-22677).
- (3) Incorporated by reference to the Current Report on Form 8-K filed on March 27, 2009 by Clariant, Inc. (SEC File No. 000-22677).