FORM 10-Q

UNITED STATES
SECURITY AND EXCHANGE COMMISSION

Washington, D.C. 20549

(Mark One)

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

For the quarterly period ended September 30, 2001

OR

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

For the transition period from _____ to _____

Commission file number 000-30171

SANGAMO BIOSCIENCES, INC.

(exact name of small business issuer as specified in its charter)

Delaware	**68-0359556**
(State or other jurisdiction of incorporation or organization)	(IRS Employer Identification No.)

501 Canal Blvd, Suite A100
Richmond, California 94804
(Address of principal executive offices)

(510) 970-6000
(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 Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days: Yes [X] No [ ]

Indicate the number of shares outstanding of each of the issuer's classes of the common stock, as of the latest practical date.

Common Stock, $.01 Par Value – 24,447,293 – shares outstanding as of September 30, 2001

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SIGNATURES

This Form 10-Q contains 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 and is subject to the safe harbors created by those sections. Statements that are forward-looking in nature should be read with caution because they involve risks and uncertainties, they are included, for example, in specific and general discussions about: our strategy; sufficiency of our cash resources; revenues from

existing and new collaborations; product development; our research and development and other expenses; our operational and legal risks; and our plans, objectives, expectations and intentions, and any other statements that are not historical facts. Actual results may differ materially from those expressed or implied in those statements. Factors that could cause these differences include, but are not limited to, those discussed under "Risk Factors" and "Management's Discussion and Analysis of Financial Condition and Results of Operations." Sangamo undertakes no obligation to publicly release any revisions to forward-looking statements to reflect events or circumstances arising after the date of this report. Readers are cautioned not to place undue reliance on the forward-looking statements, which speak only as of the date of this Quarterly Report.

PART 1. FINANCIAL INFORMATION
ITEM 1. FINANCIAL STATEMENTS

SANGAMO BIOSCIENCES, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS
(In thousands, except share and per share amounts)

	September 30, 2001 (unaudited)	December 31, 2000 (1)
Assets		
Current assets:		
Cash and cash equivalents	$ 21,205	$ 10,151
Marketable securities	42,017	53,359
Interest receivable	667	1,171
Accounts receivable	1,168	1,506
Prepaid expenses	333	325
Total current assets	65,390	66,512
Property and equipment, net	2,937	1,982
Patents, net	3,240	0
Goodwill	15,250	0
Other assets	79	431
Total assets	$ 86,896	$ 68,925
Liabilities and stockholders' equity		
Current liabilities:		
Accounts payable and accrued liabilities	$ 798	$ 634
Accrued compensation and employee benefits	662	696
Deferred revenue	688	705
Total current liabilities	2,148	2,035
Long-term liability	320	0
Total liabilities	2,468	2,035
Stockholders' equity:		
Common stock, $.01 par value, 80,000,000 shares authorized, 24,447,293 and 22,147,391 shares issued and outstanding at September 30, 2001 and December 31, 2000, respectively	127,035	89,764
Note receivable from stockholder	(16)	(463)
Deferred stock compensation	(3,340)	(4,697)
Accumulated deficit	(39,734)	(17,851)
Accumulated other comprehensive income	483	137
Total stockholders' equity	84,428	66,890
Total liabilities and stockholders' equity	$ 86,896	$ 68,925

(1) Amounts derived from Audited Statements dated December 31, 2000 filed as a part of Form 10-K

See accompanying notes.

SANGAMO BIOSCIENCES, INC.
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(In thousands, except share and per share amounts)
(Unaudited)

	Three months ended September 30,		Nine months ended September 30,	
	2000	2001	2001	2000
Revenues:				
Collaboration agreements	$ 637	$ 650	$ 2,593	$ 1,745
Federal government research grants	102	173	128	632
Total revenues	739	823	2,721	2,377
Operating expenses:				
Research and development (excludes $716 and $733 of stock based compensation expense for the three months ended September 30, 2001 and 2000, respectively, and excludes	3,892	1,896	9,150	4,977

$1,673 and $1,771 of stock based compensation expense for the nine months ended September 30, 2001 and 2000 respectively)				
General and administrative (excludes $272 and $524 of stock based compensation expense for the three months ended September 30, 2001 and 2000 respectively, and excludes $818 and $1,443 of stock based compensation expense for the nine months ended September 30, 2001 and 2000, respectively)	987	775	2,485	1,741
Stock based compensation expense	988	1,257	2,491	3,214
Acquired in-process research and development	13,062	-	13,062	1,050
Total operating expenses	18,929	3,928	27,188	10,982
Loss from operations	(18,190)	(3,105)	(24,467)	(8,605)
Interest income	783	1,287	2,584	2,483
Interest expense	-	-	-	(139)
Net loss:	$ (17,407)	$ (1,818)	$ (21,883)	$ (6,261)
Deemed dividend upon issuance of convertible preferred stock	-	-	-	1,500
Net loss attributable to common shareholders	$ (17,407)	$ (1,818)	$ (21,883)	$ (7,761)
Basic and diluted net loss per common share	$ (0.72)	$ (0.08)	$ (0.96)	$ (0.47)
Shares used in basic and diluted net loss per common share	24,320,269	21,808,649	22,869,993	16,452,464

See accompanying notes.

SANGAMO BIOSCIENCES, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(In thousands, except share and per share amounts)
(Unaudited)

	Nine months ended September 30,	
	2001	**2000**
Operating Activities:		
Net loss	$ (21,883)	$ (6,261)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	626	257
Non-cash stock compensation charges	2,491	3,214
In-process research and development	13,062	-
Issuance of common stock for technology and services rendered	-	1,050
Changes in operating assets and liabilities	791	(664)
Net cash provided by (used in) operating activities	(4,913)	(2,404)
Investing Activities:		
Maturities to and other changes in investments	11,288	(49,591)
Purchases of property and equipment	(1,581)	(1,149)
Net cash acquired in Gendaq acquisition	5,279	-
Net cash provided by (used in) investing activities	14,986	(50,740)
Financing Activities:		
Proceeds from issuance of convertible preferred stock	-	1,500
Proceeds from issuance of common stock	214	48,104
Proceeds from bank loans	320	-
Repayment of note payable	-	(250)
Proceeds from issuance of convertible debentures	-	12,637
Note receivable from stockholder	447	47
Net cash provided by financing activities	981	62,038
Net increase (decrease) in cash and equivalents	11,054	8,894
Cash and equivalents, beginning of period	10,151	251
Cash and equivalents, end of period	$ 21,205	$ 9,145
Supplemental disclosures:		
Cash paid for interest	$ -	$ 2
Noncash investing and financing activities:		
Stock options compensation	$ 2,491	$ 3,214
Deemed dividend upon issuance of convertible preferred stock	$ -	$ 1,500
Conversion of convertible debentures and accrued interest into common stock	$ -	$ 12,637
Gendaq acquisition:		
Fair value of shares and options issued	$ 36,624	$ -

See accompanying notes.

SANGAMO BIOSCIENCES, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

NOTE 1-BASIS OF PRESENTATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

BASIS OF PRESENTATION

The accompanying unaudited condensed financial statements have been prepared in accordance with generally accepted accounting principles for interim financial information and pursuant to the rules and regulations of the Securities and Exchange Commission (SEC). Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring adjustments) considered necessary for a fair presentation have been included. Operating results for the three-month and nine-month period ended September 30, 2001 are not necessarily indicative of the results that may be expected for the year ended December 31, 2001. These financial statements should be read in conjunction with the financial statements and footnotes thereto for the year ended December 31, 2000, included in Sangamo's Form 10-K as filed with the SEC.

REVENUE RECOGNITION

In December 1999, the SEC issued Staff Accounting Bulletin No. 101, "Revenue Recognition in Financial Statements" ("SAB 101"). SAB 101 summarizes the SEC's views in applying generally accepted accounting principles to revenue recognition and specifically addresses revenue recognition for up-front non-refundable fees earned in connection with research collaboration agreements. It is the SEC's interpretation that such fees should generally be recognized over the term of the agreement. Sangamo recognizes revenue in accordance with SAB 101.

Sangamo recognizes revenue from its Universal GeneToolsÔ agreements as earned when products are delivered to the Universal GeneToolsÔ collaborators and persuasive evidence of an agreement exists, the price is fixed or determinable, and collectibility is reasonably assured. Sangamo also receives research funding from Edwards Lifesciences Corporation and Renessen, LLC based on strategic partner agreements. This revenue is recognized as earned when related research services are performed over the course of the agreements.

Payments to fund research activities made under strategic partnering agreements are recognized over the period that Sangamo performs research services. Amounts paid in advance under such agreements are deferred until the research services are performed. Sangamo's federal government research grants provide for the reimbursement of qualified expenses for research and development as defined under the terms of the grant agreement. Revenue under grant agreements is recognized when the related research expenses are incurred. Grant reimbursements are received on a quarterly or monthly basis and are subject to the issuing agency's right of audit. Revenue associated with performance milestones is recognized based upon the achievement of milestones, as defined in the respective agreements.

NOTE 2-BASIC AND DILUTED NET LOSS PER SHARE

Net loss per share is presented under the requirements of Financial Accounting Standards Board ("FAS") No. 128, "Earnings per Share." Basic loss per share is computed based on the weighted average shares of common stock outstanding (excluding shares subject to repurchase) and excludes any effects of options, warrants, and convertible securities. Potentially dilutive securities such as options, warrants, and convertible preferred stock have been excluded from the computation of diluted net loss per share, as their effect is antidilutive.

In thousands, except per common share amounts	Three months ended September 30,		Nine months ended September 30,	
	2001	2000	2001	2000
Historical:				
Net loss attributable to common stockholders	$ (17,407)	$ (1,818)	$ (21,883)	$ (7,761)
Basic and diluted:				
Weighted-average shares of common stock outstanding	24,424	22,071	22,997	16,715
Less: weighted-average shares subject to repurchase	(104)	(262)	(127)	(263)
Shares used in computing basic and diluted net loss per common share	24,320	21,809	22,870	16,452
Basic and diluted net loss per common share	$ (0.72)	$ (0.08)	$ (0.96)	$ (0.47)

NOTE 3- STOCK COMPENSATION

During the years ended December 31, 2000, 1999, and 1998, in connection with the grant of stock options to employees and directors, Sangamo recorded deferred stock compensation totaling $6.8 million, $1.5 million, and $780,000, respectively, representing the difference between the fair value of common stock on the date such options were granted and the exercise price. These amounts are included as a reduction of stockholders' equity and are being amortized over the vesting period of the individual options, generally four years, using an accelerated vesting method. The accelerated vesting method provides for vesting of portions of the overall award at interim dates and results in higher vesting in earlier years than straight-line vesting. The fair value of Sangamo common stock for purposes of this calculation was determined based on the business factors underlying the value of common stock on the date such option grants were made. Sangamo recorded stock compensation charges of $988,000 and $1.3 million in the three-month period ended September 30, 2001 and 2000, respectively. During the nine months periods ended September 30, 2001 and 2000, Sangamo recorded stock compensation charges of $2.5 million and $3.2 million, respectively. At September 30, 2001, Sangamo had a total of $3.4 million remaining to be amortized over the vesting periods of the employee stock options. The Company also recorded deferred compensation of $685,000 during the third quarter of 2001 related to options issued to Gendaq employees. This amount will be amortized as the options vest over the next several years.

Sangamo also recognizes compensation expense related to options granted to directors and consultants. Such options are valued based on the fair value of the Sangamo's common stock when the options vest. During the three and nine months ended September 30, 2001, respectively, of the total $988,000 and $2.5 million in stock-based compensation charges, $107,000 and $450,000 was recorded as options granted to consultants vested.

NOTE 4-COMPREHENSIVE LOSS

Comprehensive loss is comprised of net loss and other comprehensive income (loss). Other comprehensive income (loss) includes certain changes in stockholders' equity that are excluded from net loss, which includes unrealized gains and losses on our available-for-sale securities and foreign currency translation adjustments. Comprehensive loss and its components for the three- and nine-month periods ended September 30, 2001 and 2000 are as follows (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2001	2000	2001	2000
Net loss	$ (17,407)	$ (1,818)	$ (21,883)	$ (6,261)
Changes in unrealized (loss) gain on securities available-for-sale	91	(83)	236	(83)
Foreign currency translation adjustment	110	-	110	-
Comprehensive loss	$ 201	$ -	$ 346	$ -

NOTE 5-DEEMED DIVIDEND UPON ISSUANCE OF CONVERTIBLE PREFERRED STOCK

In January 2000, Sangamo sold 333,333 shares of its Series C convertible preferred stock to an investor for net proceeds of $1.5 million. Subsequent to the commencement of the initial public offering process, Sangamo re-evaluated the fair value of its stock as of January 2000 and determined it to be more than the issue price of $4.50 per share. Accordingly, the incremental fair value, limited to the amount of the proceeds received of $1.5 million, is deemed to be the equivalent of a preferred stock dividend. Sangamo recorded the deemed dividend at the date of issuance by offsetting charges and credits to preferred stock, without any effect on total stockholders' equity. The preferred stock dividend increases the loss applicable to common stockholders in the calculation of basic net loss per share for the nine-month period ended September 30, 2000. There were no deemed dividends recorded during the nine months ended September 30, 2001.

NOTE 6-STRATEGIC PARTNERSHIP

In January 2000, Sangamo announced that it had entered into a strategic partner agreement with Edwards Lifesciences Corporation, formerly the CardioVascular Group of Baxter Healthcare Corporation for the development of ZFP TFs in cardiovascular and peripheral vascular diseases. Under this agreement, Edwards purchased a $5 million convertible note which converted into common stock at the time of the company's initial public offering at the IPO price, and Sangamo received $1 million in initial research funding from Edwards which was recorded as deferred revenue and was recognized as revenue as related research services were performed over the research period of one year. In March 2000, Edwards purchased a $7.5 million convertible note and received a right of first refusal for three years to negotiate a license for additional ZFP-TherapeuticsÔ in cardiovascular and peripheral vascular diseases. This note also converted into common stock upon consummation of the company's initial public offering at the IPO price. In January 2001, Edwards provided a further $1 million in research funding which was recorded as deferred revenue and is being recognized as revenue as related research services are performed. In the future, Sangamo may receive option fees, milestone payments, royalties and additional research funding from this agreement.

NOTE 7-ACQUISITION OF GENDAQ, LTD

On July 4, 2001, Sangamo BioSciences, Inc. ("Sangamo") completed its acquisition of the outstanding shares of Gendaq Limited ("Gendaq"), a private company located in the United Kingdom in a purchase business combination (the "Agreement"). Gendaq scientists have focused their research efforts on regulating genes through the engineering of transcription factors known as zinc finger DNA-binding proteins (ZFPs).

Pursuant to the Agreement, Sangamo issued 2,124,638 shares of its common stock in exchange for 100% of the outstanding shares of Gendaq's common stock. Sangamo has also reserved a total of 125,366 shares for issuance upon exercise of outstanding Gendaq stock options, which were assumed in the transaction.

Sangamo's total cost to acquire Gendaq is approximately $36.7 million based on a fair value of $16.41 per share of Sangamo's common stock. The stock price used to value the securities issued is based on an average price during the few days before and after May 30, 2001, the day Sangamo and Gendaq announced an agreement under which Sangamo received an option to purchase all of the outstanding stock of Gendaq on agreed upon terms.

The cost to acquire Gendaq has been allocated to the assets acquired and liabilities assumed according to their respective fair values, with the excess purchase price being allocated to goodwill. The allocation of the aggregate purchase price is based in part on an independent valuation analysis, which was obtained for purposes of allocating the fair value of purchased assets and assumed liabilities.

The estimated purchase cost of Gendaq is as follows:

Value of securities issued	$ 34,873,808
Assumption of Gendaq's common stock options, less intrinsic value of unvested options of $684	(1,049,618)
Estimated transaction costs and expenses	781,436
Total	$ 36,704,862

The purchase price allocation is as follows:

	Amount	Useful Life *(In years)*	Annual Amortization of Intangibles
Net tangible assets of Gendaq	$ 5,033,826		
Intangible assets acquired:			
Patents	3,359,623	7	$ 479,946
In-process research and development	13,061,500	--	
Goodwill	15,249,913	--	
Total purchase price allocation	$ 36,704,862		$ 479,946

In-process research and development represents that portion of the purchase price of the acquisition related to the research and development activities which: (i) have not demonstrated their technological feasibility, and (ii) have no alternative future uses. Sangamo recognized an expense of $13.1 million upon consummation of the transaction.

The amount of in-process research and development was determined based on an analysis using the risk-adjusted cash flows expected to be generated by the products that result from the in-process projects. The analysis included forecasted future cash flows that were expected to result from the progress made on each of the in-process projects prior to the purchase dates. These cash flows were estimated by first forecasting, on a product-by-product basis, total revenues expected from sales

of the first generation of each in-process product, as well as expected expenses to complete in process research and development for each project. Appropriate operating expenses and cash flow adjustments were deducted from the forecast to establish projected net cash flows for the in process technology. Finally, these net returns were discounted to a present value at discount rates that incorporate both the weighted average cost of capital (relative to the biotechnology industry and the Company) as well as the product-specific risk associated with the purchased in-process research and development products. The product-specific risk factors included each product in each phase of development, type of molecule under development, likelihood of regulatory approval, manufacturing process capability, scientific rationale, pre-clinical safety and efficacy data, target product profile and development plan. The overall discount rate used for the purchase valuation ranged from 35% to 50% depending upon the stage of completion of each product and the risks associated with each, which represents a significant risk premium to our weighted average cost of capital.

The forecast data in the analysis was based on internal product level forecast information maintained by management in the ordinary course of managing the business. The inputs used in analyzing in-process research and development were based on assumptions, which management believed to be reasonable but which were inherently uncertain and unpredictable. These assumptions may be incomplete or inaccurate, and no assurance can be given that unanticipated events and circumstances will not occur.

A brief description of projects that were included in the in-process research and development charge is set forth below. Projects subsequently added to the research and development pipeline are not included. Since the acquisition date, there have been no significant changes to the phase of development for the projects listed. Management estimated that research and development expenditures of at least $30 to $35 million will be required to complete the in-process projects.

Project	Description / Indication	Phase of Development	Estimated Substantial Completion Date	Fair Value (in millions)
HIV	Therapeutic product candidate	Pre-clinical	2008	1.9
Anti-Inflammatory	Therapeutic product candidate	Pre-clinical	2007	3.4
EPO	Therapeutic product candidate	Pre-clinical	2007	0.9
Insulin	Therapeutic product candidate	Pre-clinical	2009	1.2
Functional Genomics	Gene regulation product	Pre-marketing	2002	3.2
Agriculture	Gene regulation product	Pre-marketing	2005	2.5

The following table represents unaudited pro forma results of operations as if the Gendaq acquisition had occurred at the beginning of each period presented using the purchase method.

Gendaq's financial information included in these pro forma results is derived from its nine months ended September 30, 2001 and 2000 unaudited financial statements. Gendaq's financial information as of all dates and for all periods presented have been adjusted, where appropriate, to present Gendaq's financial position and results of operations in accordance with accounting principles generally accepted in the United States.

The unaudited pro forma condensed combined financial information is presented for illustrative purposes only and is not necessarily indicative of the operating results or financial positions that would have occurred if the transaction had been consummated at the dates indicated, nor is it necessarily indicative of future operating results or financial position of the combined companies and should not be construed as representative of these amounts for any future dates or periods. Loss from operations and net loss excludes in-process research and development expense due to its non-recurring nature.

In thousands, except share and per share amounts	Nine months ended September 30	
	Pro Forma 2001	Pro Forma 2000
Total revenues	$ 2,877	$ 2,377
Loss from operations	$ 13,066	$ (8,498)
Net loss	$ 10,464	$ (6,122)
Basic and diluted net loss per share	$ (0.43)	$ (0.33)
Shares used to compute basic and diluted loss per share	24,294,289	18,577,105

NOTE 8: RECENTLY ISSUED ACCOUNTING STANDARDS

The Financial Accounting Standards Board issued Financial Accounting Standards No. 141, Business Combinations, and No. 142, Goodwill and Other Intangible Assets, in the latter half of July, 2001. Statement 141 prohibits the use of the pooling-of-interests method for business combinations initiated after June 30, 2001. Statement 141, which also includes the criteria for the recognition of intangible assets separately from goodwill, is effective for any business combination accounted for by the purchase method that is completed after June 30, 2001. Statement 142, which includes the requirements to test goodwill and indefinite lived intangible assets for impairment rather than amortize them, will be effective for fiscal years beginning after December 15, 2001. As a result of the transition rules, goodwill and certain intangible assets acquired in transactions completed after June 30, 2001 will not be amortized. Therefore, allocated goodwill resulting from the purchase price allocation of Gendaq will not be amortized, but will be subject to a review of impairment.

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

Overview

Sangamo, which was incorporated in 1995, is a leader in the research, development, and commercialization of transcription factors for the regulation of gene expression. Our Universal Gene Recognition™ platform is a proprietary technology based on engineering a naturally occurring class of transcription factors referred to as zinc finger DNA-binding protein transcription factors, or ZFP TFs. We believe that Universal Gene Recognition™ is a fundamentally enabling technology, widely applicable to pharmaceutical discovery, development of human therapeutics, plant agriculture, industrial biotechnology, and clinical diagnostics. We intend to commercialize our technology broadly over its many applications. In July 2001, Sangamo acquired Gendaq Limited, a private company located in the United Kingdom focused on the regulation of genes using zinc finger DNA-binding proteins.

From our inception through September 30, 2001, our activities related primarily to establishing a research and development organization and developing relationships with our corporate collaborators. We have incurred net losses since inception and expect to incur losses in the future as we expand our research and development activities. To date, we have funded our operations primarily through the issuance of equity securities, borrowings, payments from federal government research grants, and from corporate collaborators and strategic partners. As of September 30, 2001, we had an accumulated deficit of $39.9 million.

Our revenues consist primarily of revenues from our corporate partners for ZFP TFs, federal government research grant funding, and payments from strategic partners for committed research funding and research milestone payments. Since September 1998, Sangamo has signed collaborative research agreements with a total of 22 corporate partners for Universal GeneToolsÔ engineered zinc finger proteins. In January 2000, we announced the initiation of a therapeutic product development collaboration with Edwards Lifesciences Corporation. Under the agreement, we have licensed to Edwards on a worldwide, exclusive basis, ZFP-Therapeutics™ for use in the activation of Vascular Endothelial Growth Factor (VEGF) and VEGF receptors in cardiovascular and peripheral vascular diseases. We will be responsible for advancing product candidates into preclinical animal testing. Edwards will be responsible for preclinical development, regulatory affairs, clinical development and the sales and marketing of the ZFP-Therapeutic™ products. In the future, we may receive up to $26 million in milestone payments in connection with the development and commercialization of the first product under this agreement. Sangamo will also receive royalties on product sales. There is no assurance that the companies will achieve our development and commercialization milestones. Edwards has the right to terminate the agreement at any time upon 90 days written notice. In the event of termination, we retain all payments previously received.

Sangamo's losses to date have resulted principally from costs incurred in research and development, general and administrative costs associated with operations, non-cash stock-based compensation expenses associated with stock options granted to employees and consultants from January 1997 through the closing of our initial public offering in April 2000, and non-cash charges associated with the Gendaq business combination.

Research and development expenses consist primarily of salaries and related personnel expenses, subcontracted research expenses, and technology license expenses. As of September 30, 2001, all research and development costs have been expensed as incurred. We believe that continued investment in research and development is critical to attaining our strategic objectives. We expect these expenses will increase significantly in the future as we continue to develop our Universal Gene RecognitionÔ technology platform.

General and administrative expenses consist primarily of salaries and related personnel expenses for executive, finance and administrative personnel, professional fees, and other general corporate expenses. As we add personnel and incur additional costs related to the growth of our business, general and administrative expenses will also increase.

Sangamo's quarterly operating results will depend on a number of factors, including the delivery of products to corporate partners, the signing or expiration of contracts with corporate partners or government research grants, our success rate in achieving milestones with corporate partners, and the timing and willingness of collaborators to commercialize products which would result in royalties. As a consequence, quarterly operating results have fluctuated in the past and are likely to do so in the future.

RESULTS OF OPERATIONS

Three Months ended September 30, 2001 and 2000

Total revenues. Total revenues consist of revenues from corporate collaboration agreements and federal government research grants. Total revenues decreased to $739,000in the three months ended September 30, 2001 from $823,000 in the corresponding period in 2000. Revenues from our collaboration agreements were $637,000 in the three months ended September 30, 2001, compared with $650,000 in the corresponding period in 2000. Federal government research grant revenues were $102,000 in the three months ended September 30, 2001, compared to $173,000 in the corresponding period in 2000. The decrease in the three months ended September 30, 2001 was principally due to completion of federal research government grants during prior quarters. We plan to continue to apply for federal government research grants in the future to support the development of applications of our technology platform. Although we have received grants in the past, we cannot assure you that applications will result in receipt of grants in the future.

Research and development expenses. Research and development expenses were $4.6 million for the three months ended September 30, 2001 as compared to $2.6 million in the corresponding period in 2000. Non-cash research and development expenses in the third quarter in 2001 included $716,000 for stock-based deferred compensation charges, as compared to $733,000 for deferred compensation during the same quarter in 2000. Excluding the non-cash charges, total third quarter 2001 research and development expenses were $3.9 million as compared to $1.9 million in the corresponding period in 2000. The increase in the 2001 period was primarily for additional employee related expenses as we increased our scientific staffing levels, including the expenses of Gendaq, acquired in July 2001. We expect research and development expenses to increase significantly in future periods, particularly as we continue to increase the scientific staff to continue to develop the Universal Gene RecognitionÔ technology and to meet the needs of our corporate collaborators, and as we begin to incur additional costs associated with the Gendaq acquisition.

General and administrative expenses. General and administrative expenses remained at $1.3 million in the three months ended September 30, 2001, as compared to $1.3 million during the corresponding period in 2000. Non-cash administrative expenses in the third quarter of 2001 were $272,000 for a stock-based deferred compensation charge compared to $524,000 for deferred compensation during the same quarter of 2000. Excluding the non-cash charges, total third quarter 2001 general and administrative expenses were $987,000 as compared to $775,000 in 2000. The increase was primarily attributable to increased labor costs to support our expanded research and development activities and development of our Universal Gene RecognitionÔ technology. We expect that general and administrative expenses will increase in the future to support continued growth of our research, development and commercialization efforts.

In-process research and development expenses. On July 4, 2001, Sangamo completed its acquisition of the outstanding shares of Gendaq, a private company located in the United Kingdom, in a purchase business combination. Of Sangamo's total cost of $36.7 million to acquire Gendaq, $13.1 million was expensed as research and development in the third quarter.

In-process research and development represents that portion of the purchase price of the acquisition related to the research and development activities which: (i) have not demonstrated their technological feasibility, and (ii) have no alternative future uses. Sangamo recognized an expense of $13.1 million upon consummation of the transaction.

The amount of in-process research and development was determined based on an analysis using the risk-adjusted cash flows expected to be generated by the products that result from the in-process projects. The analysis included forecasted future cash flows that were expected to result from the progress made on each of the in-process projects prior to the purchase dates. These cash flows were estimated by first forecasting, on a product-by-product basis, total revenues expected from sales of the first generation of each in-process product, as well as expected expenses to complete in process research and development for each project. Appropriate operating expenses and cash flow adjustments were deducted from the forecast to establish projected net cash flows for the in process technology. Finally, these net returns were discounted to a present value at discount rates that incorporate both the weighted average cost of capital (relative to the biotechnology industry and the Company) as well as the product-specific risk associated with the purchased in-process research and development products. The product-specific risk factors

included each product in each phase of development, type of molecule under development, likelihood of regulatory approval, manufacturing process capability, scientific rationale, pre-clinical safety and efficacy data, target product profile and development plan. The overall discount rate used for the purchase valuation ranged from 35% to 50% depending upon the stage of completion of each product and the risks associated with each, which represents a significant risk premium to our weighted average cost of capital.

The forecast data in the analysis was based on internal product level forecast information maintained by management in the ordinary course of managing the business. The inputs used in analyzing in-process research and development were based on assumptions, which management believed to be reasonable but which were inherently uncertain and unpredictable. These assumptions may be incomplete or inaccurate, and no assurance can be given that unanticipated events and circumstances will not occur.

A brief description of projects that were included in the in-process research and development charge is set forth below.. Projects subsequently added to the research and development pipeline are not included. Since the acquisition date, there have been no significant changes to the phase of development for the projects listed. Management estimated that research and development expenditures of at least $30 to $35 million will be required to complete the in-process projects.

Project	Description / Indication	Phase of Development	Estimated Substantial Completion Date	Fair Value (in millions)
HIV	Therapeutic productcandidate	Pre-clinical	2008	1.9
Anti-Inflammatory	Therapeutic product candidate	Pre-clinical	2007	3.4
EPO	Therapeutic product candidate	Pre-clinical	2007	0.9
Insulin	Therapeutic product candidate	Pre-clinical	2009	1.2
Functional Genomics	Gene regulation product	Pre-marketing	2002	3.2
Agriculture	Gene regulation product	Pre-marketing	2005	2.5

Interest income (expense), net. Net interest income decreased from $1.3 millionin the three months ended September 30, 2000 to $783,000 in the corresponding period in 2001. The decrease in interest income resulted from lower average interest-bearing balances resulting from our continued losses from operations, as well as lower interest rates.

Nine Months ended September 30, 2001 and 2000

Total revenues. Total revenues consist of revenues from corporate collaboration agreements and federal government research grants. Total revenues increasedto $2.7 million in the nine months ended September 30, 2001 from $2.4 million in the corresponding period in 2000. Revenues from collaboration agreements were $2.6 million in the nine months ended September 30, 2001, compared with $1.7 million in the corresponding period in 2000. The increasein the nine months ended September 30, 2001 was principally attributable to revenues recognized under new Universal Genetools agreements and a strategic collaboration agreement with Renessen, LLC a joint venture between Cargill and Monsanto Company. Federal government research grant revenues were $128,000 in the nine months ended September 30, 2001, compared to $632,000 in the corresponding period in 2000, a decrease of $504,000. The decrease in the nine months ended September 30, 2001 was principally due to completion of federal research government grants during prior periods. We plan to continue to apply for federal government research grants in the future to support the development of applications of our technology platform. Although we have received grants in the past, we cannot assure you that applications will result in successful grants in the future.

Research and development expenses. Research and development expenses were $10.8 million for the nine months ended September 30, 2001 as compared to $7.8 million in the corresponding period in 2000. Non-cash research and development expenses in the nine month period ended September 30, 2000 were $2.8 million including a one-time expense of approximately $1.0 million for the issuance of common stock related to the in-licensing of certain in-process technology and a stock-based deferred compensation charges of $1.8 million, as compared to $1.7 million deferred compensation during the same period in 2001. Excluding the non-cash charges, total research and development expenses in the 2001 period were $9.1 million as compared to $6.0 million in the corresponding period in 2000. The increase in the 2001 period was primarily for additional employee related expenses as we increased our scientific staffing levels, as well as the inclusion of the consolidated results of Gendaq, Ltd. from the date of acquisition in July. We expect research and development expenses to increase significantly in future periods, particularly as we continue to increase the scientific staff to continue to develop the Universal Gene RecognitionÔ technology and to meet the needs of our corporate collaborators.

General and administrative expenses. General and administrative expenses increased from $3.2 million in the nine months ended September 30, 2000 to $3.3 million in the corresponding period in 2001. Non-cash administrative expenses in the nine month period ended September 30, 2000 included $1.4 million in stock-based deferred compensation charge compared to $818,000 for deferred compensation during the same period of 2001. Excluding the non-cash charges, total general and administrative expenses in the 2000 period were $1.7 million as compared to $2.5 million in the corresponding period in 2001. The increase was primarily attributable to increased labor costs to support our expanded research and development activities and development of our Universal Gene RecognitionÔ technology and costs associated with being a public company. We expect that general and administrative expenses will increase in the future to support continued growth of our research, development and commercialization efforts.

In-process research and development expenses. The in-process research and development expenses for the nine-months ended September 30, 2001 are described under the three-month ended discussion and analysis.

Interest income (expense), net. Net interest income increased to $2.6 million in the nine months ended September 30, 2001 from $2.3 million in the corresponding period in 2000. The increase in net interest income resulted from higher average interest-bearing balances during 2001.

Liquidity and Capital Resources

Since inception, Sangamo has financed operations primarily through sales of preferred and common stock, including our initial public offering in April 2000, federal government research grants, payments from corporate collaborators, and other financing activities such as a bank line of credit. As of September 30, 2001 we had cash, cash equivalents, short and long-term investments totaling $63.9 million.

We used $4.9 million for operating activities in the nine months ended September 30, 2001. This consisted of the net loss for the period of $21.9 million offset by non-cash charges of $16.2 million relating to compensation expenses and in-process research and development charges relating to the Gendaq acquisition, as well as other changes in operating assets and liabilities. Investing activities provided $14.9 million as marketable securities totaling $11.3 million matured and were reclassified as cash equivalents balanced by $1.6 million invested in leasehold improvements and capital equipment purchases. In addition, we acquired $5.3 million in cash as a result of our purchase of Gendaq. Net cash provided by financing activities in the period was $981,000 primarily from the issuance of common shares and debt financing.

We believe that the net proceeds of the Company's initial public offering, together with available cash resources and funds received from corporate collaborators are sufficient to finance our existing operations for at least two years. Our capital requirements depend upon a number of factors, including our ability to increase our revenues from corporate partners and government grants, and the level and timing of our research and development expenditures. We expect to devote substantial capital resources to the development of our Universal Gene RecognitionÔ technology platform over the next several years. We may need to raise substantial additional capital to fund subsequent operations. Funding, however, may not be available on favorable terms, if at all.

Quantitative and Qualitative Disclosures about Market Risk

Our exposure to market risk for changes in interest rates relates primarily to our cash equivalents and investments. The investments are classified as available for sale. We do not use derivative financial instruments in our investment portfolio. We attempt to ensure the safety and preservation of our invested funds by limiting default and market risks. Our cash and investments policy emphasizes liquidity and preservation of principal over other portfolio considerations. We select investments that maximize interest income to the extent possible within these guidelines. We satisfy liquidity requirements by investing excess cash in securities with different maturities to match projected cash needs and limit concentration of credit risk by diversifying our investments among a variety of high credit-quality issuers. We mitigate default risk by investing in only investment-grade securities. The portfolio includes marketable securities with active secondary or resale markets to ensure portfolio liquidity. All investments have a fixed interest rate and are carried at market value, which approximates cost. If market interest rates were to increase by 1 percent from September 30, 2001, the fair value of our portfolio would decline by approximately $100,000. The modeling technique used measures the change in fair values arising from an immediate hypothetical shift in market interest rates and assumes ending fair values include principal plus accrued interest.

The following table represents the fair value balance of our cash, cash equivalents and marketable investments by year of expected maturity that are subject to interest rate risk as of September 30, 2001 (in thousands, except for interest rates):

	2001	2002
Cash equivalents	**$ 21,205**	**$ -**
Average interest rates	**3.23%**	**-**
Marketable securities, including accrued interest receivable	**$ 26,456**	**$ 16,228**
Average interest rates	**4.46%**	**6.79%**

RISK FACTORS

An investment in our common stock is risky. You should carefully consider the following risks, as well as the other information contained in this report. If any of the following risks actually occurs, it would harm our business. In that case, the trading price of our common stock could decline, and you might lose all or a part of your investment. The risks and uncertainties described below are not the only ones facing us. Additional risks and uncertainties not presently known to us or that we currently see as immaterial, may also harm our business.

Risks Related to Our Business

Our gene regulation technology is unproven and if we are unable to use this technology in all our intended applications, it would limit our revenue opportunities.

Our technology involves new and unproven approaches to gene regulation. Although we have generated some ZFP TFs for some gene sequences, we have not created ZFP TFs for all gene sequences and we may not be able to create ZFP TFs for all gene sequences which would limit the usefulness of our technology. In addition, while we have demonstrated the function of engineered ZFP TFs in mammalian cell culture, yeast, insects, plants and animals, we have not done so in humans and many other organisms, and the failure to do so could restrict our ability to develop commercially viable products. If we and our Universal GeneTools™ collaborators or strategic partners are unable to extend our results to new gene sequences and experimental animal models, we may be unable to use our technology in all its intended applications. Also, delivery of ZFP TFs into cells in these and other environments is limited by a number of technical challenges, which we may be unable to surmount.

The utility of our ZFP TFs is in part based on the belief that the regulation of gene expression may help scientists better understand the role of human, animal, plant and other genes in drug discovery, as well as therapeutic, diagnostic, agricultural and industrial biotechnology applications. There is only a limited understanding of the role of genes in all these fields. Life sciences companies have developed or commercialized only a few products in any of these fields based on results from genomic research or the ability to regulate gene expression. We, our Universal GeneTools™ collaborators or our strategic partners may not be able to use our technology to identify and validate drug targets or other targets in order to develop commercial products.

If our technology does prove to be effective, it still may not lead to commercially viable products, which would reduce our revenue opportunities.

Even if our Universal GeneTools™ collaborators or strategic partners are successful in identifying drug targets or other targets based on discoveries made using our ZFP TFs, they may not be able to discover or develop commercially viable products or may determine to pursue products that do not use our technology. To date, no company has developed or commercialized any therapeutic, diagnostic, agricultural or industrial biotechnology products based on our technology. The failure of our technology to provide safe, effective, useful or commercially viable approaches to the discovery and development of these products would significantly limit our business plan and future growth.

Initial evaluations of our engineered ZFP TFs delivered to our Universal GeneTools™ collaborators have produced mixed results.

Some of our Universal GeneTools™ collaborators were unable to substantiate the effects of our gene regulation technology. Generally, failures were re-evaluated at Sangamo using our current approach of examining the local chromatin structure for accessible sites and then targeting ZFP TFs to these areas. In most cases, additional ZFP TFs were designed and tested for these targets, and data was generated at Sangamo, or by our partners, confirming the ability to regulate these targets. Sangamo performs this more extensive validation on all Universal GeneTools™ targets prior to use by external parties. However, there can be no assurances that we will be able to regulate all gene targets, and repression of a gene is usually more difficult than activation. Although we have been able to achieve repression in numerous genes, the degree of repression may not be sufficient to permit our collaborators to realize their objectives. For example, one of our collaborators has advised us that while some of our ZFP TFs delivered to them repressed certain target gene sequences to a significant extent the repression was not complete enough to warrant proceeding to develop revised ZFP TFs for this purpose. However, this collaborator has advised us that positive results were achieved using our ZFP TFs to regulate other target gene sequences. In addition, some of our collaborators have not yet generated the final results of their testing, and no assurances can be given that our collaborators will be able to achieve satisfactory results. These ZFP TFs, or ones engineered in the future, may not function as intended. If we are unsuccessful in engineering ZFP TFs that achieve positive results for our collaborators or strategic partners, this would significantly harm our business by reducing our revenues.

If our competitors develop, acquire or market technologies or products that are more effective than ours, this would reduce or eliminate our commercial opportunity.

Any products that we or our collaborators or strategic partners develop using our Universal Gene Regulation™ technology platform will participate in highly competitive markets. Even if we are able to generate ZFP TFs that achieve useful results, competing technologies may prove to be more effective or less expensive which would limit or eliminate our revenue opportunities. Competing technologies may include other methods of regulating gene expression. Universal Gene Recognition™ has broad application in the life sciences, and competes with a broad array of new technologies and approaches being applied to genetic research by many companies. Competitive technologies include those used to analyze the expression of genes in cells or tissues, determine gene function, discover new genes, analyze genetic information and regulate genes. Our competitors include biotechnology companies with:

- competing proprietary technology;
- substantially greater capital resources than ours;
- larger research and development staffs and facilities than ours;
- greater experience in product development and in obtaining regulatory approvals and patent protection; and
- greater manufacturing and marketing capabilities than we do.

These organizations also compete with us to:

- attract qualified personnel;
- attract parties for acquisitions, joint ventures or other collaborations; and
- license the proprietary technologies of academic and research institutions that are competitive with our technology which may preclude us from pursuing similar opportunities.

Accordingly, our competitors may succeed in obtaining patent protection or commercializing products before us. In addition, any products that we develop may compete with existing products or services that are well established in the marketplace.

Failure to attract, retain and motivate skilled personnel and cultivate key academic collaborations will delay our product development programs and our research and development efforts.

We are a small company with 96 employees as of September 30, 2001 and our success depends on our continued ability to attract, retain and motivate highly qualified management and scientific personnel, and our ability to develop and maintain important relationships with leading academic and other research institutions and scientists. Competition for personnel and academic and other research collaborations is intense. The success of our technology development programs depends on our ability to attract and retain highly trained personnel. If we lose the services of personnel with these types of skills, it could impede significantly the achievement of our research and development objectives. If we fail to negotiate additional acceptable collaborations with academic and other research institutions and scientists, or if our existing collaborations are unsuccessful, our technology development programs may be delayed or may not succeed.

At present the scope of our needs is somewhat limited to the expertise of personnel who are able to engineer ZFP TFs and apply them to gene regulation. In the future, we will need to hire additional personnel and develop additional academic collaborations as we continue to expand our research and development activities and to work on some of our planned projects because these activities and projects will require additional expertise in disciplines applicable to the products we would develop with them. Further, our planned activities will require existing management to develop additional expertise. We do not know if we will be able to attract, retain or motivate the required personnel to achieve our goals.

We may have difficulty managing our growth, which may slow our growth rate or give rise to inefficiencies which would reduce our profits.

We have recently experienced, and expect to continue to experience, growth in the number of our employees and the scope of our operating and financial systems. This growth has resulted in an increase in responsibilities for both existing and new management personnel. Our ability to manage growth effectively will require us to continue to implement and improve our operational, financial and management information systems and to recruit, train, motivate and manage our employees. We may not be able to manage our growth and expansion, and the failure to do so may slow our growth rate or give rise to inefficiencies which would reduce our profits.

If we are unable to successfully integrate our recent acquisition of Gendaq Limited or any future acquisition, our business would suffer.

In July 2001, we acquired Gendaq Limited, a London-based biotechnology company. In connection with the acquisition, we acquired all of the business of Gendaq including a research team of 16 scientists, 22 patent applications and two issued patents. Acquisitions of this type involve a number of risks, including:

- difficulties in assimilating the operations and employees of the acquired company;
- diversion of management's attention from ongoing business concerns;
- difficulties in incorporating the acquired technology and rights into our research and product offerings;
- maintenance of uniform standards, controls procedures and policies; and
- additional expense associated with charges allocated to in-process research and development.

Acquisitions are likely to result in a dilutive issuance of equity securities. For example, we issued common stock and replacement stock options in connection with our acquisition of Gendaq. We cannot assure you that any acquisition will enhance our future commercial success or generate sufficient net revenues to offset the associated costs of the acquisition.

We may experience difficulty in managing our international operations.

Our subsidiary, Gendaq Limited, is located in London and is incorporated under the laws of the United Kingdom. Because we do not have experience in managing international subsidiaries, we may experience difficulty in managing our new international operations.

We are at an early stage of development and may not succeed or become profitable.

We began operations in 1995 and are at an early stage of development. We have incurred significant losses to date, and our revenues have been generated from federal government research grants, Universal GeneTools™ collaborators and strategic partners. Our Universal GeneTools™ collaborators are evaluating our ZFP TFs. If the ZFP TFs do not provide sufficient value to those collaborators, then they may not continue to work with us. This may also impair our ability to attract additional collaborators. As a result, our business is subject to all of the risks inherent in the development of a new technology, which includes the need to:

- attract additional new Universal GeneTools™ collaborators and strategic partners and expand existing relationships;
- attract and retain qualified scientific and technical staff and management, particularly scientific staff with expertise to further apply and develop our early stage technology;
- attract and enter into research collaborations with academic and other research institutions and scientists;

- obtain sufficient capital to support the expense of developing our technology platform and developing, testing and commercializing products;
- develop a market for our products; and
- successfully transition from a company with a research focus to a company capable of supporting commercial activities.

In addition to competitive pressures, problems frequently encountered with research, development and commercialization of new technologies and products will likely affect us. Most of our ZFP TF design and testing procedures take place on a relatively small scale. In the future, we intend to apply ZFP TF design and testing procedures at a scale involving hundreds of genes per year. We may not be able to successfully or efficiently achieve this scale. In addition, while we have had success in applying ZFP TF gene regulation in our laboratories, we may have difficulty in transferring our technology to our collaborators' and strategic partners' laboratories.

We anticipate continuing to incur operating losses for at least two years. If material losses continue for a longer period, we may be unable to continue our operations.

We have generated operating losses since we began operations in 1995. The extent of our future losses and the timing of profitability are highly uncertain, and we may not be profitable in the foreseeable future. We have been engaged in developing our Universal Gene Recognition™ technology since inception, which has and will continue to require significant research and development expenditures. To date, we have generated our revenues from federal government research grants, Universal GeneTools™ collaboration agreements and strategic partnership agreements. As of September 30, 2001, we had an accumulated deficit of approximately $39.9 million. Even if we succeed in increasing our current product and research revenue or developing additional commercial products, we expect to incur losses in the near future and may continue to incur losses for at least the next two years. These losses may increase as we expand our research and development activities. If the time required to generate significant product revenues and achieve profitability is longer than we currently anticipate, we may not be able to sustain our operations.

We may require additional financing. If we are unable to obtain this financing, we will be unable to develop our technology and products.

We do not know whether we will require additional financing, or that, if acquired, it will be on terms favorable to our stockholders or us. We have consumed substantial amounts of cash to date and expect capital outlays and operating expenditures to increase over the next several years as we expand our infrastructure and research and development activities. We may raise this financing through public or private financings or additional Universal GeneTools™ collaborations, strategic partnerships or licensing arrangements. If additional financing becomes necessary in the future, it would likely be at least tens of millions of dollars.

While we believe our current financial resources should be adequate to sustain our operations for two years, it is not possible to estimate our financial requirements thereafter. However, to the extent we concentrate our efforts on proprietary human therapeutics, we will require FDA approval and extensive clinical trials of our potential products. This process may cost in excess of $100 million per product.

Factors beyond our control could cause our quarterly results to fluctuate.

We believe that period-to-period comparisons of our results of operations are not necessarily meaningful and should not be relied upon as indicators of future performance. The variability of receipt of funds from corporate partners, as well as the implementation of new accounting pronouncements, may lead to quarterly fluctuations in our revenue. We generally operate with limited backlog in our Universal GeneTools™ business because our ZFP TFs are typically designed and engineered as orders are received. As a result, product sales in any quarter are generally dependent on orders received and shipped in that quarter. Universal GeneTools™ sales are also difficult to forecast because demand varies substantially from customer to customer and from period to period. While strategic partnerships may provide us with committed quarterly research funding, the signing of such deals, and the subsequently initiation of revenue recognition, is also uncertain.

Due to all of the foregoing factors, it is possible that in one or more future quarters our results may fall below the expectations of public market analysts and investors. In such event, the trading price of our common stock would likely be adversely impacted.

Our Universal GeneTools™ collaboration agreements with companies are of limited scope, and if we are not able to expand the scope of our existing collaborations or enter into new ones, our revenues will be negatively impacted and our research initiatives may be slowed or halted.

Our Universal GeneTools™ collaborations are important to us because they permit us to introduce our technology to many companies by supplying them with a specified ZFP TF for a payment without licensing any of our technology. The collaboration agreements, however, are of limited scope. Under most of our current Universal GeneTools™ collaborations we receive a payment for supplying ZFP TFs for gene targets specified by the companies. These companies are not obligated to make continuing payments to us in connection with their research efforts or to pursue any product development program with us. As a result, we may not develop long-term relationships with these companies that could lead to additional revenues. If we are not able to expand the scope of our existing collaborations or enter into new ones, we may have reduced revenues and be forced to slow or halt research initiatives.

Commercialization of our technologies depends on strategic partnering with other companies, and if we are not able to find strategic partners in the future, we may not be able to develop our technologies or products, which could slow our growth and decrease our revenues.

We expect to rely, to some extent, on our strategic partners to provide funding in support of our research and to perform some independent research, preclinical and clinical testing. Our technology is broad based and we do not currently possess the resources necessary to develop and commercialize potential products that may result from our technologies, or the resources or capabilities to complete any approval processes that may be required for the products, therefore we must enter into additional strategic partnerships to develop and commercialize products. Of the thousands of ZFP TFs which target specific genes, our current collaborators and strategic partners are working with less than 100, therefore in order to fully utilize our ZFP transcriptions factors we would need a number of new Universal GeneTools™ collaborators and strategic partners to accomplish our research.

We may require significant time to secure additional collaborations or strategic partners because we need to effectively market the benefits of our technology to these future collaborators and strategic partners, which uses the time and efforts of research and development personnel and our management. Further, each collaboration or strategic partnering arrangement will involve the negotiation of terms that may be unique to each collaborator or strategic partner. These business development efforts may not result in a collaboration or strategic partnership.

If we do not enter into additional strategic partnering agreements, we will experience reduced revenues and may not develop or commercialize our products. The loss of our current or any future strategic partnering agreement would not only delay or terminate the potential development or commercialization of any products we may derive from our technologies but also delay or terminate our ability to test ZFP TFs for specific genes. If any strategic partner fails to conduct the collaborative activities successfully and in a timely manner, the preclinical or clinical development or commercialization of the affected product candidates or research programs could be delayed or terminated.

Our existing strategic partnering agreements are, and we would expect any future arrangement to be based on the achievement of milestones. Under the strategic partnering agreements, we expect to receive revenue for the research and development of products based on achievement of specific milestones. Achieving these milestones will depend, in part, on the efforts of our strategic partner as well as our own. In contrast, our current Universal GeneTools™ collaboration agreements only pay us to supply ZFP TFs for the collaborator's independent use, rather than for future results of the collaborator's efforts. If we or any strategic partner fails to meet specific milestones, then the strategic partnership can be terminated which could decrease our revenues.

Our Universal GeneTools™ collaborators and strategic partners may decide to adopt alternative technologies or may be unable to develop commercially viable products using our technology, which would negatively impact our revenues and our strategy to develop these products.

Our collaborators or strategic partners may adopt alternative technologies of our competitors which could decrease the marketability of our technology. Because many of our Universal GeneTools™ collaborators or strategic partners are likely to be working on more than one research project, they could choose to shift their resources to projects other than those they are working on with us. If they do so, that would delay our ability to test our technology and would delay or terminate the development of potential products based on our gene regulation technology. Further, our collaborators and strategic partners may elect not to develop products arising out of our collaborative and strategic partnering arrangements or to devote sufficient resources to the development, manufacturing, marketing or sale of these products. If any of these events occur, we may not be able to develop our technologies or commercialize our products.

We may be unable to license gene transfer technologies that we may need to commercialize our Universal Gene Recognition™ technology.

In order to regulate an endogenous gene, the ZFP TF must be delivered to a cell. We have licensed certain gene transfer technology for use with our Universal GeneTools™ in pharmaceutical discovery. We are evaluating this and other technologies which may need to be used in the delivery of ZFP TFs into cells for *in vitro* and *in vivo* applications. However, we may not be able to license the gene transfer technologies required to develop and commercialize our Universal Gene Recognition™ technology. We have not developed our own gene transfer technologies and rely on our ability to enter into license agreements to provide us with rights to the necessary gene transfer technology. The inability to obtain a license to use gene transfer technologies with entities which own such technology on reasonable commercial terms, if at all, could delay or prevent the preclinical evaluation, clinical testing and/or commercialization of our therapeutic product candidates.

We intend to conduct proprietary research programs to discover therapeutic product candidates. These programs increase our risk of product failure, may significantly increase our research expenditures, and may involve conflicts with our collaborators and strategic partners.

Conducting proprietary research programs may not generate corresponding revenue and may create conflicts with our collaborators or strategic partners. The implementation of this strategy will involve substantially greater business risks and the expenditure of significantly greater funds than our current research activities. In addition, these programs will require substantial commitments of time from our management and staff. Moreover, we have no experience in preclinical or clinical testing, obtaining regulatory approval or commercial-scale manufacturing and marketing of therapeutic products, and we currently do not have the resources or capability to manufacture therapeutic products on a commercial scale. In order for us to commercialize these products directly, we would need to develop, or obtain through outsourcing arrangements, the capability to execute all of these functions, market and sell products. We do not have these capabilities, and we may not be able to develop or otherwise obtain the requisite preclinical, clinical, regulatory, manufacturing, marketing and sales capabilities.

In addition, disagreements with our Universal GeneTools™ collaborators or strategic partners could develop over rights to our intellectual property with respect to our proprietary research activities. Any conflict with our collaborators or strategic partners could reduce our ability to enter into future collaboration or strategic partnering agreements and negatively impact our relationship with existing collaborators and strategic partners, which could reduce our revenue and delay or terminate our product development.

Because it is difficult and costly to protect our proprietary rights, and third parties have filed patent applications that are similar to ours, we cannot ensure the proprietary protection of our technologies and products.

Our commercial success will depend in part on obtaining patent protection of our technology and successfully defending these patents against third-party challenges. The patent positions of pharmaceutical and biotechnology companies can be highly uncertain and involve complex legal and factual questions. No consistent policy regarding the breadth of claims allowed in biotechnology patents has emerged to date. Accordingly, we cannot predict the breadth of claims allowed in patents we own or license.

We are a party to various license agreements that give us rights under specified patents and patent applications. Our current licenses, and our future licenses, will contain performance obligations. If we fail to meet those obligations, the licenses could be terminated. If we are unable to continue to license these technologies on commercially reasonable terms, or at all, we may be forced to delay or terminate our product development and research activities.

With respect to our present and any future sublicenses, since our rights derive from those granted to our sublicensor, we are subject to the risk that our sublicensor may fail to perform its obligations under the master license or fail to inform us of useful improvements in, or additions to, the underlying intellectual property owned by the original licensor.

We are unable to exercise the same degree of control over intellectual property that we license from third parties as we exercise over our internally developed intellectual property. We generally do not control the prosecution of patent applications that we license from third parties; therefore, the patent applications may not be prosecuted in a timely manner.

- The degree of future protection for our proprietary rights is uncertain and we cannot ensure that:
- we or our licensors were the first to make the inventions covered by each of our pending patent applications;
- we or our licensors were the first to file patent applications for these inventions;
- others will not independently develop similar or alternative technologies or reverse engineer any of our products, processes or technologies;
- any of our pending patent applications will result in issued patents;
- any patents issued or licensed to us or our Universal GeneTools™ collaborators or strategic partners will provide a basis for commercially viable products or will provide us with any competitive advantages or will not be challenged and invalidated by third parties;
- we will develop additional products, processes or technologies that are patentable; or
- the patents of others will not have an adverse effect on our ability to do business.

Others have filed and in the future are likely to file patent applications that are similar to ours. We are aware that there are academic groups and other companies that are attempting to develop technology which is based on the use of zinc finger and other DNA-binding proteins, and that these groups and companies have filed patent applications. Several patents have been issued, although Sangamo has no current plans to use the associated inventions. More particularly, we are aware of pending patent applications with claims directed to zinc finger libraries and methods of designing zinc finger DNA-binding proteins. These applications are not issued patents. If the pending claims were granted in their present form, however, they could interfere with our right to commercialize our products and processes. If these or other patents issue, it is possible that the holder of any patent or patents granted on these applications may bring an infringement action against our collaborators, strategic partner or us claiming damages and seeking to enjoin commercial activities relating to the affected products and processes. The costs of litigating the claim could be substantial. Moreover, we cannot predict whether our Universal GeneTools™ collaborators, strategic partners or we would prevail in any actions. In addition, if the relevant patent claims were upheld as valid and enforceable and our products or processes were found to infringe the patent or patents, we could be prevented from making, using or selling the relevant product or process unless we could obtain a license or were able to design around the patent claims. While we believe that our proprietary intellectual property would give us substantial leverage to secure a cross-license, it is uncertain that any license required under that patent or patents would be made available on commercially acceptable terms, if at all. We believe that there may be significant litigation in the genomics industry regarding

patent and other intellectual property rights which could subject us to litigation. If we become involved in litigation, it could consume a substantial portion of our managerial and financial resources.
We rely on trade secrets to protect technology where we believe patent protection is not appropriate or obtainable. Trade secrets, however, are difficult to protect. While we require employees, academic collaborators and consultants to enter into confidentiality agreements, we may not be able to adequately protect our trade secrets or other proprietary information or enforce these confidentiality agreements.

Our Universal GeneTools™ collaborators, strategic partners and scientific advisors have rights to publish data and information in which we may have rights. If we cannot maintain the confidentiality of our technology and other confidential information in connection with our collaborations and strategic partnerships, then we may not be able to receive patent protection or protect our proprietary information.

Our potential therapeutic products are subject to a lengthy and uncertain regulatory process, and if these potential products are not approved, we will not be able to commercialize those products.

The FDA must approve any therapeutic and some diagnostic products based on ZFP TF technology before it can be marketed in the United States. The process for receiving regulatory approval is long and uncertain, and even if we had a potential product, this product may not withstand the rigors of testing under the regulatory approval processes. Before commencing clinical trials in humans, we must submit and receive approval from the FDA of an Investigational New Drug Application. Clinical trials are subject to oversight by institutional review boards and the FDA, and these trials must meet particular conditions, such that they:

- must be conducted in conformance with the FDA's good clinical practice regulations;
- must meet requirements for institutional review board oversight;
- must meet requirements for informed consent;
- are subject to continuing FDA oversight;
- may require large numbers of test subjects; and
- may be suspended by us or the FDA at any time if it is believed that the subjects participating in these trials are being exposed to unacceptable health risks or if the FDA finds deficiencies in the Investigational New Drug application or the conduct of these trials.

We must also demonstrate that the product is safe and effective in the patient population that will be treated. Data obtained from preclinical and clinical activities are susceptible to varying interpretations that could delay, limit or prevent regulatory clearances. In addition, we may encounter delays or rejections based upon additional government regulation from future legislation or administrative action or changes in FDA policy during the period of product development, clinical trials and FDA regulatory review. Failure to comply with applicable FDA or other applicable regulatory requirements may result in criminal prosecution, civil penalties, recall or seizure of products, total or partial suspension of production or injunction, as well as other regulatory action against our potential products or us. Additionally, we have no experience in conducting and managing the clinical trials necessary to obtain regulatory approval.

In addition, we may also require approval from the Recombinant DNA Advisory Committee, or RAC, which is the advisory board to the National Institutes of Health, or NIH, focusing on clinical trials involving gene transfer.

We have not submitted an application with the FDA or any other regulatory authority for any product candidate, and neither the FDA nor any other regulatory authority has approved any therapeutic, diagnostic, agricultural or industrial product candidate developed with our technology for commercialization in the United States or elsewhere.

Regulatory approval, if granted, may be limited to specific uses or geographic areas which could limit our ability to generate revenues.

Regulatory approval may limit the indicated use for which we can market a product. Further, once regulatory approval for a product is obtained, it and its manufacturer are subject to continual review. Discovery of previously unknown problems with a product or manufacturer may result in restrictions on the product, manufacturer and manufacturing facility, including withdrawal of the product from the market. In Japan and Europe, regulatory agencies also set or approve prices.

Even if regulatory clearance of a product is granted, this clearance is limited to those specific states and conditions for which the product is useful as demonstrated through clinical trials. We cannot ensure that any therapeutic product developed by us, alone or with others, will prove to be safe and effective in clinical trials and will meet all of the applicable regulatory requirements needed to receive marketing clearance.

Outside the United States, our ability to market a product is contingent upon receiving a marketing authorization from the appropriate regulatory authorities so we cannot predict whether or when we would be permitted to commercialize our product. These foreign regulatory approval processes include all of the risks associated with FDA clearance described above.

Laws or public sentiment may limit our production of genetically engineered agricultural products in the future, and these laws could reduce our ability to sell these products.

Genetically engineered products are currently subject to public debate and heightened regulatory scrutiny, either of which could prevent or delay production of agricultural products. We may develop genetically engineered agricultural products for ourselves or with our strategic partners. The field testing, production and marketing of genetically engineered plants and plant products are subject to federal, state, local and foreign governmental regulation. Regulatory agencies administering existing or future regulations or legislation may not allow production and marketing of our genetically engineered products in a timely manner or under technically or commercially feasible conditions. In addition, regulatory action or private litigation could result in expenses, delays or other impediments to our product development programs or the commercialization of resulting products.
The FDA currently applies the same regulatory standards to foods developed through genetic engineering as applied to foods developed through traditional plant breeding. Genetically engineered food products, however, will be subject to premarket review if these products raise safety questions or are deemed to be food additives. Governmental authorities could also, for social or other purposes, limit the use of genetically engineered products created with our gene regulation technology.

Even if we are able to obtain regulatory approval of genetically engineered products, our success will also depend on public acceptance of the use of genetically engineered products including drugs, plants and plant products. Claims that genetically engineered products are unsafe for consumption or pose a danger to the environment may influence public attitudes. Our genetically engineered products may not gain public acceptance. The subject of genetically modified organisms has received negative publicity in Europe, which has aroused public debate. The adverse publicity in Europe could lead to greater regulation and trade restrictions on imports of genetically altered products. If similar adverse public reaction occurs in the United States, genetic research and its resulting products could be subject to greater domestic regulation and could decrease the demand for our technology and products.

If conflicts arise between us and our collaborators, strategic partners, scientific advisors or directors, these parties may act in their self-interest, which may limit our ability to implement our strategies.

If conflicts arise between us and our corporate or academic collaborators, strategic partners or scientific advisors or directors, the other party may act in its self-interest which may limit our ability to implement our strategies. Some of our Universal GeneTools™ or academic collaborators or strategic partners are conducting multiple product development efforts within each area that is the subject of the collaboration with us. Generally, in each of our collaborations, we have agreed not to conduct independently, or with any third party, any research that is competitive with the research conducted under our collaborations. Our collaborations may cause us to limit the areas of research that we pursue, either alone or with others. Our collaborators or strategic partners, however, may develop, either alone or with others, products in related fields that are competitive with the products or potential products that are the subject of these collaborations. Competing products, either developed by the collaborators or strategic partners or to which the collaborators or strategic partners have rights, may result in their withdrawal of support for our product candidates.

Some of our collaborators or strategic partners could also become competitors in the future. Our collaborators or strategic partners could develop competing products, preclude us from entering into collaborations with their competitors, fail to obtain timely regulatory approvals, terminate their agreements with us prematurely or fail to devote sufficient resources to the development and commercialization of products. Any of these developments could harm our product development efforts.

Our collaborations with outside scientists may be subject to change which could limit our access to their expertise.

We work with scientific advisors and collaborators at academic research institutions. These scientists are not our employees and may have other commitments that would limit their availability to us. Although our scientific advisors generally agree not to do competing work, if a conflict of interest between their work for us and their work for another entity arises, we may lose their services. Although our scientific advisors and academic collaborators sign agreements not to disclose our confidential information, it is possible that some of our valuable proprietary knowledge may become publicly known through them.

If we use biological and hazardous materials in a manner that causes injury or violates laws, we may be liable for damages.

Our research and development activities involve the controlled use of potentially harmful biological materials as well as hazardous materials, chemicals and various radioactive compounds. We cannot completely eliminate the risk of accidental contamination or injury from the use, storage, handling or disposal of these materials. In the event of contamination or injury, we could be held liable for damages that result, and any liability could exceed our resources. We are subject to federal, state and local laws and regulations governing the use, storage, handling and disposal of these materials and specified waste products. The cost of compliance with these laws and regulations could be significant.

Anti-takeover provisions in our certificate of incorporation and Delaware law could prevent a potential acquiror from buying your stock.

Anti-takeover provisions of Delaware law, in our certificate of incorporation and equity benefit plans may make a change in control of our company more difficult, even if a change in control would be beneficial to our stockholders. These provisions may allow our board of directors to prevent or make changes in the management and control of our company. In particular, our board of directors will be able to issue up to 5,000,000 shares of preferred stock with rights and privileges that might be senior to our common stock, without the consent of the holders of the common stock. Further, without any further vote or action on the part of the stockholders, the board of directors will have the authority to determine the price, rights, preferences, privileges and restrictions of the preferred stock. This preferred stock, if it is ever issued, may have preference over and harm the rights of the holders of common stock. Although the issuance of this preferred stock will provide us with flexibility in connection with possible acquisitions and other corporate purposes, this issuance may make it more difficult for a third party to acquire a majority of our outstanding voting stock. Similarly, our authorized but unissued common stock is available for future issuance without stockholder approval.

In addition, our certificate of incorporation:

- states that stockholders may not act by written consent but only at a stockholders' meeting;
- establishes advance notice requirements for nominations for election to the board of directors or proposing matters that can be acted upon at stockholders' meetings; or
- limits who may call a special meeting of stockholders.

Our stock price may be volatile, which could result in substantial losses for investors.

Volatility in the biotechnology market could cause you to incur substantial losses. An active public market for our common stock may not be sustained and the market price of our common stock may become highly volatile. The market prices of securities of biotechnology companies are currently highly volatile. The market price of our common stock may fluctuate significantly in response to the following factors, some of which are beyond our control:

- changes in market valuations of similar companies;
- announcements by us or our competitors of new or enhanced products, technologies or services or significant contracts, acquisitions, strategic relationships, joint ventures or capital commitments;
- regulatory developments;
- additions or departures of key personnel;
- deviations in our results of operations from the estimates of securities analysts; and
- future sales of our common stock or other securities.

Insiders have substantial control over Sangamo and could delay or prevent a change in corporate control.

The interest of management could conflict with the interest of our other stockholders. Our executive officers, directors and principal stockholders beneficially own, in the aggregate, approximately 63 percent of our outstanding common stock. As a result, these stockholders, if they choose to act together, will be able to exercise control over all matters requiring stockholder approval, including the election of directors and approval of significant corporate transactions. This could have the effect of delaying or preventing a change of control of Sangamo, which in turn could reduce the market price of our stock.

PART II. OTHER INFORMATION

Item 2. Changes in Securities and Use of Proceeds

The effective date of our first Registration Statement on Form S-1 filed under the Securities Act of 1933, as amended, relating to the initial public offering of our common stock was April 6, 2000. On the same date, we signed an underwriting agreement with Lehman Brothers, Chase H&Q, ING Barings LLC, and William Blair & Co., the managing underwriters for the initial public offering and the representatives of the underwriters named in the underwriting agreement, for the initial public offering of 3,500,000 shares of our common stock at an initial public offering price of $15 per share. The offering commenced on April 6, 2000 and was closed on April 11, 2000. The initial public offering resulted in gross proceeds of $52.5 million. We received net proceeds of $48.8 million after deducting underwriting

discounts of $3.7 million. Expenses related to the offering totaled approximately $1.4 million. None of Sangamo's net proceeds of the Offering were paid directly or indirectly to any director, officer, general partner of Sangamo or their associates, persons owning 10% or more of any class of equity securities of Sangamo, or an affiliate.

From the time of receipt through September 30, 2001, Sangamo has used the net proceeds from its initial public offering of common stock to invest in short-term and long-term, interest bearing, investment-grade securities and has used its existing cash balances to fund the general operations. The proceeds will be used for general corporate purposes, including working capital and product development. A portion of the net proceeds will also be used to acquire or invest in complementary businesses or products or to obtain the right to use complementary technologies. Sangamo has no agreements or commitments with respect to any such acquisition or investments and is not currently engaged in any material negotiations with respect to any such transaction.

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

Reports: Sangamo filed a Current Report on Form 8-K dated July 17, 2001 as amended on August 17, 2001 describing, pursuant to Item 2 and Item 7, the completion of its acquisition of Gendaq Limited.

SIGNATURES

Pursuant to the requirements of the Securities and Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

SANGAMO BIOSCIENCES, INC. Dated: October 19, 2001

/s/ Edward O. Lanphier II

Edward O. Lanphier II
President, Chief Executive Officer

/s/ Shawn K. Johnson

Shawn K. Johnson
Senior Director of Finance
Principal Accounting Officer