UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

# FORM 10-Q

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

For the quarterly period ended June 28, 2003

or

[ ] Transition report pursuant to section 13 or 15(d) of the Securities Exchange Act of 1934 for the transition period from

________________ to ________________

Commission file number 0-20852

ULTRALIFE BATTERIES, INC.
(Exact name of registrant as specified in its charter)

| Delaware | 16-1387013 |
|---|---|
| (State or other jurisdiction of incorporation or organization) | (I.R.S. Employer Identification No.) |

2000 Technology Parkway, Newark, New York   14513
(Address of principal executive offices) (Zip Code)

(315) 332-7100
(Registrant's telephone number, including area code)

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

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

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act). Yes ..... No ...X...

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.
Common stock, $.10 par value - 13,146,294 shares of common stock outstanding, net of 727,250 treasury shares, as of June 28, 2003.

ULTRALIFE BATTERIES, INC.
INDEX


| | | Page |
|---|---|---|
| PART I | FINANCIAL INFORMATION | |
| Item 1. | Financial Statements (Unaudited) | |
| | Condensed Consolidated Balance Sheets - June 28, 2003 and December 31, 2002 | 3 |
| | Condensed Consolidated Statements of Operations - Three and six months ended June 28, 2003 and June 30, 2002 | 4 |
| | Condensed Consolidated Statements of Cash Flows - Six months ended June 28, 2003 and June 30, 2002 | 5 |
| | Notes to Consolidated Financial Statements | 6 |
| Item 2. | Management's Discussion and Analysis of Financial Condition and Results of Operations | 16 |
| Item 3. | Quantitative and Qualitative Disclosures About Market Risks | 24 |
| Item 4. | Controls and Procedures | 24 |
| PART-II | OTHER INFORMATION | |

Item 1. Legal Proceedings.................................................. 26

Item 2. Changes in Securities and Use of Proceeds........................ 27

Item 4. Submission of Matters to a Vote of Securities Holders............ 27

Item 6. Exhibits and Reports on Form 8-K................................. 28

Signatures....................................................... 29

CEO and CFO Certifications....................................... 30

Item 1. Financial Statements

ULTRALIFE BATTERIES, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS
(Dollars in Thousands, Except Per Share Amounts)
(unaudited)

| ASSETS | June 28, 2003 | December 31, 2002 |
|---|---|---|
| Current assets: | | |
| Cash and cash equivalents | $ 1,612 | $ 1,322 |
| Available-for-sale securities | 2 | 2 |
| Restricted cash | 50 | 50 |
| Trade accounts receivable (less allowance for doubtful accounts of $215 at June 28, 2003 and $297 at December 31, 2002) | 13,140 | 6,200 |
| Inventories | 6,729 | 5,813 |
| Prepaid expenses and other current assets | 1,110 | 968 |
| Total current assets | 22,643 | 14,355 |
| Property, plant and equipment | 17,260 | 15,336 |
| Other assets: | | |
| Investment in UTI | 1,550 | 1,550 |
| Technology license agreements (net of accumulated amortization of $1,368 at June 28, 2003 and $1,318 at December 31, 2002) | 83 | 133 |
| | 1,633 | 1,683 |
| Total Assets | $ 41,536 | $ 31,374 |
| LIABILITIES AND SHAREHOLDERS' EQUITY | | |
| Current liabilities: | | |
| Short-term debt and current portion of long-term debt | $ 3,256 | $ 816 |
| Accounts payable | 7,065 | 4,283 |
| Other current liabilities | 3,220 | 2,045 |
| Total current liabilities | 13,541 | 7,144 |
| Long-term liabilities: | | |
| Debt and capital lease obligations | 953 | 1,354 |
| Grant | 750 | 633 |
| | 1,703 | 1,987 |
| Commitments and contingencies (Note 10) | | |
| Shareholders' equity: | | |
| Preferred stock, par value $0.10 per share, authorized 1,000,000 shares; none outstanding | -- | -- |
| Common stock, par value $0.10 per share, authorized 40,000,000 shares issued - 13,873,544 at June 28, 2003 and 13,579,519 at December 31, 2002) | 1,387 | 1,358 |
| Capital in excess of par value | 116,876 | 115,251 |
| Accumulated other comprehensive loss | (1,081) | (1,016) |
| Accumulated deficit | (88,512) | (90,972) |
| | 28,670 | 24,621 |
| Less -- Treasury stock, at cost -- 727,250 shares | 2,378 | 2,378 |
| Total shareholders' equity | 26,292 | 22,243 |
| Total Liabilities and Shareholders' Equity | $ 41,536 | $ 31,374 |

The accompanying Notes to Consolidated Financial Statements are an integral part of these statements.

ULTRALIFE BATTERIES, INC.
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(Dollars in Thousands, Except Per Share Amounts)
(unaudited)

| | Three Months Ended | | Six Months Ended | |
|---|---|---|---|---|
| | June 28, 2003 | June 30, 2002 | June 28, 2003 | June 30, 2002 |
| Revenues | $20,110 | $ 8,578 | $35,538 | $ 17,440 |
| Cost of products sold | 15,379 | 7,493 | 27,648 | 15,433 |
| Gross margin | 4,731 | 1,085 | 7,890 | 2,007 |
| Operating expenses: | | | | |
| Research and development | 646 | 1,099 | 1,231 | 2,137 |
| Selling, general, and administrative | 2,187 | 1,755 | 4,149 | 3,736 |
| Impairment of long-lived assets | -- | 14,318 | -- | 14,318 |
| Total operating expenses | 2,833 | 17,172 | 5,380 | 20,191 |
| Operating income (loss) | 1,898 | (16,087) | 2,510 | (18,184) |
| Other income (expense): | | | | |
| Interest income | 4 | 3 | 5 | 6 |
| Interest expense | (150) | (106) | (242) | (207) |
| Equity loss in UTI | -- | (678) | -- | (1,179) |
| Miscellaneous | 397 | 362 | 187 | 265 |
| Income (loss) before income taxes | 2,149 | (16,506) | 2,460 | (19,299) |
| Income taxes | -- | -- | -- | -- |
| Net income (loss) | $ 2,149 | $(16,506) | $ 2,460 | $(19,299) |
| Earnings (loss) per share - basic | $ 0.17 | $ (1.28) | $ 0.19 | $ (1.52) |
| Earnings (loss) per share - diluted | $ 0.16 | $ (1.28) | $ 0.19 | $ (1.52) |
| Weighted average shares outstanding - basic | 12,927 | 12,920 | 12,895 | 12,662 |
| Weighted average shares outstanding - diluted | 13,651 | 12,920 | 13,266 | 12,662 |

The accompanying Notes to Consolidated Financial Statements are an integral part of these statements.

ULTRALIFE BATTERIES, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Dollars in Thousands)
(unaudited)

| | Six Months Ended | |
|---|---|---|
| | June 28, 2003 | June 30, 2002 |
| OPERATING ACTIVITIES | | |
| Net income (loss) | $ 2,460 | $(19,299) |
| Adjustments to reconcile net income (loss) to net cash used in operating activities: | | |
| Depreciation and amortization | 1,504 | 2,131 |
| Foreign exchange gains | (192) | (265) |
| Equity loss in UTI | -- | 1,179 |
| Non-cash stock-based compensation | 26 | -- |
| Impairment of long-lived assets | -- | 14,318 |
| Changes in operating assets and liabilities: | | |
| Accounts receivable | (6,940) | (1,623) |
| Inventories | (916) | 826 |
| Prepaid expenses and other current assets | (142) | 286 |
| Accounts payable and other current liabilities | 3,957 | (483) |
| Net cash used in operating activities | (243) | (2,930) |
| INVESTING ACTIVITIES | | |
| Purchase of property and equipment | (3,278) | (792) |
| Proceeds from sale leaseback | -- | 451 |
| Purchase of securities | -- | 666 |
| Sales of securities | -- | 1,399 |
| Net cash (used in) provided by investing activities | (3,278) | 1,724 |
| FINANCING ACTIVITIES | | |
| Change in revolving credit facilities | 2,440 | -- |
| Proceeds from issuance of common stock | 1,128 | 2,350 |
| Proceeds from issuance of debt | 500 | 600 |
| Principal payments on long-term debt and capital lease obligations | (401) | (506) |
| Proceeds from grant | 117 | -- |
| Net cash provided by financing activities | 3,784 | 2,444 |
| Effect of exchange rate changes on cash | 27 | 72 |
| Increase in cash and cash equivalents | 290 | 1,310 |
| Cash and cash equivalents at beginning of period | 1,322 | 706 |
| Cash and cash equivalents at end of period | $ 1,612 | $ 2,016 |
| SUPPLEMENTAL CASH FLOW INFORMATION | | |
| Interest paid | $ 116 | $ 266 |

The accompanying Notes to Consolidated Financial Statements are an integral part of these statements.

ULTRALIFE BATTERIES, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Dollar Amounts in Thousands - Except Share and Per Share Amounts)
(unaudited)

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## 1. BASIS OF PRESENTATION

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with generally accepted accounting principles for interim financial information and with the instructions to Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals and adjustments) considered necessary for a fair presentation of the condensed consolidated financial statements have been included. Results for interim periods should not be considered indicative of results to be expected for a full year. Reference should be made to the consolidated financial statements contained in the Company's Transition Report on Form 10-K for the six-month period ended December 31, 2002.

As of July 1, 2002, the Company changed its monthly closing schedule, moving to a weekly-based cycle as opposed to a calendar month - based cycle. While the actual dates for the quarter-ends will change slightly each year, the Company believes that there will not be any material differences when making quarterly comparisons.

Effective December 31, 2002, the Company changed its fiscal year-end from June 30 to December 31.

Certain amounts in the prior years' consolidated financial statements have been reclassified to conform to the current year presentation.

## 2. IMPAIRMENT OF LONG-LIVED ASSETS

In June 2002, the Company reported a $14,318 impairment charge. This impairment charge related to a writedown of long-lived assets in the Company's rechargeable production operations, reflecting a change in the Company's strategy. Changes in external economic conditions culminated in June 2002, reflecting a slowdown in the mobile electronics marketplace and a realization that near-term business opportunities utilizing the high volume rechargeable production equipment had dissipated. These changes caused the Company to shift away from high volume polymer battery production to higher value, lower volume opportunities. The Company's redefined strategy eliminates the need for its high volume production line that had been built mainly to manufacture Nokia cell phone replacement batteries. The new strategy is a three-pronged approach. First, the Company will manufacture in-house for the higher value, lower volume polymer rechargeable opportunities. Second, the Company will utilize its affiliate in Taiwan, Ultralife Taiwan, Inc., as a source for both polymer and liquid lithium cells. And third, the Company will look to other rechargeable cell manufacturers as sources for cells that the Company can then assemble into completed battery packs.

The impairment charge was accounted for under Financial Accounting Standard No. 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of", which requires evaluating the assets' carrying value based on future cash flows. As a result of the impairment of the Company's fixed assets, depreciation charges were reduced by approximately $1,800 per year.

3. EARNINGS (LOSS) PER SHARE

Basic earnings per share are calculated by dividing net income by the weighted average number of common shares outstanding during the period. Diluted earnings per share are calculated by dividing net income, adjusted for interest on convertible securities, by potentially dilutive common shares, which include stock options, warrants and convertible securities.

Net loss per share is calculated by dividing net loss by the weighted average number of common shares outstanding during the period. The impact of conversion of dilutive securities, such as stock options and warrants, are not considered where a net loss is reported as the inclusion of such securities would be anti-dilutive. As a result, basic loss per share is the same as diluted loss per share.

The computation of basic and diluted earnings per share is summarized as follows:

| (In thousands, except per share data) | Three Months Ended | | Six Months Ended | |
|---|---|---|---|---|
| | June 28, 2003 | June 30, 2002 | June 28, 2003 | June 30, 2002 |
| Net Income (a) | $2,149 | ($16,506) | $2,460 | ($19,299) |
| Effect of Dilutive Securities: | | | | |
| Stock Options / Warrants | 44 | -- | 44 | -- |
| Convertible Note | 6 | -- | 9 | -- |
| Net Income - Adjusted (b) | $2,199 | ($16,506) | $2,513 | ($19,299) |
| Average Shares Outstanding - Basic (c) | 12,927 | 12,920 | 12,895 | 12,662 |
| Effect of Dilutive Securities: | | | | |
| Stock Options / Warrants | 557 | -- | 246 | -- |
| Convertible Note | 167 | -- | 125 | -- |
| Average Shares Outstanding - Diluted (d) | 13,651 | 12,920 | 13,266 | 12,662 |
| EPS - Basic (a/c) | $0.17 | ($1.28) | $0.19 | ($1.52) |
| EPS - Diluted (b/d) | $0.16 | ($1.28) | $0.19 | ($1.52) |

The Company also had the equivalent of 618,000 and 2,514,000 options and warrants outstanding for the three-month periods ended as of June 28, 2003 and June 30, 2002, respectively, and 974,000 and 2,277,000 options and warrants outstanding for the six-month periods ended as of June 28, 2003 and June 30, 2002, respectively, which were not included in the computation of diluted EPS because these securities would have been anti-dilutive for the periods presented.

4. STOCK-BASED COMPENSATION

The Company has various stock-based employee compensation plans. The Company applies Accounting Principles Board (APB) Opinion No. 25, "Accounting for Stock Issued to Employees," and related interpretations which require compensation costs to be recognized based on the difference, if any, between the quoted market price of the stock on the grant date and the exercise price. As all options granted to employees under such plans had an exercise price at least equal to the market value of the underlying common stock on the date of grant, and given the fixed nature of the equity instruments, no stock-based employee compensation cost is reflected in net income (loss). The effect on net income (loss) and earnings per share if the Company had applied the fair value

recognition provisions of Statement of Financial Accounting Standards ("SFAS") No. 148, "Accounting for Stock-Based Compensation - Transition and Disclosure, an Amendment of SFAS No. 123" (as discussed below in Note 12 - Recent Accounting Pronouncements), to stock-based employee compensation is as follows:

| | Three Months Ended | | Six Months Ended | |
|---|---|---|---|---|
| | June 28, 2003 | June 30, 2002 | June 28, 2003 | June 30, 2002 |
| Net income (loss), as reported | $2,149 | $(16,506) | $2,460 | $(19,299) |
| Add: Stock-based employee compensation expense included in reported net income (loss), net of related tax effects | -- | -- | -- | -- |
| Deduct: Total stock-based employee compensation expense determined under fair value based method for all awards, net of related tax effects | (317) | (356) | (540) | (652) |
| Pro forma net income (loss) | $1,832 | $(16,862) | $1,920 | $(19,951) |
| Earnings (loss) per share: | | | | |
| Basic - as reported | $0.17 | $(1.28) | $0.19 | $(1.52) |
| Basic - pro forma | $0.14 | $(1.31) | $0.15 | $(1.58) |
| Diluted - as reported | $0.16 | $(1.28) | $0.19 | $(1.52) |
| Diluted - pro forma | $0.13 | $(1.31) | $0.14 | $(1.58) |

5. COMPREHENSIVE INCOME (LOSS)

The components of the Company's total comprehensive income (loss) were:

| | Three Months Ended | | Six Months Ended | |
|---|---|---|---|---|
| | June 28, 2003 | June 30, 2002 | June 28, 2003 | June 30, 2002 |
| Net income (loss) | $2,149 | $(16,506) | $2,460 | $(19,299) |
| Foreign currency translation adjustments | (124) | 2 | (65) | (21) |
| Total comprehensive income (loss) | $2,025 | $(16,504) | $2,395 | $(19,320) |

6. INVENTORIES

Inventories are stated at the lower of cost or market with cost determined under the first-in, first- out (FIFO) method. The composition of inventories was:

| | June 28, 2003 | December 31, 2002 |
|---|---|---|
| Raw materials | $4,603 | $3,259 |
| Work in process | 2,045 | 1,882 |
| Finished goods | 1,101 | 1,207 |
| | 7,749 | 6,348 |
| Less: Reserve for obsolescence | 1,020 | 535 |
| | $6,729 | $5,813 |

7. PROPERTY, PLANT AND EQUIPMENT

Major classes of property, plant and equipment consisted of the following:

| | June 28, 2003 | December 31, 2002 |
|---|---|---|
| Land | $123 | $ 123 |
| Buildings and leasehold improvements | 1,625 | 1,619 |
| Machinery and equipment | 30,306 | 28,772 |
| Furniture and fixtures | 338 | 319 |
| Computer hardware and software | 1,474 | 1,405 |
| Construction in progress | 2,135 | 291 |
| | 36,001 | 32,529 |
| Less: Accumulated depreciation | 18,741 | 17,193 |
| | $17,260 | $15,336 |

8. DEBT

In November 2001, the Company received approval for a $750 grant/loan from a federally sponsored small cities program. The grant/loan has assisted in funding capital expansion plans that the Company expects will lead to job creation. The Company has been reimbursed for approved capital as it incurred the cost. In August 2002, the $750 small cities grant/loan documentation was finalized and the Company was reimbursed approximately $400 for costs it had incurred to date for equipment purchases applicable under this grant/loan. By the end of March 2003, all $750 had been advanced to the Company. During the first quarter of 2003, $117 under this grant/loan was reimbursed as the Company incurred additional expenses and submitted requests for reimbursement. If the Company meets its employment quota requirements by April 1, 2005, the loan and all associated accrued interest will be forgiven. If the Company does not meet its employment quota requirements, then the funds advanced and the associated interest will be converted into a loan that will be repaid over a seven-year period. The Company has initially recorded the proceeds from this grant/loan as a long-term liability and will record these proceeds as income as the certainty of meeting the employment criteria become definitive. Interest has been accrued at a rate of 5% per year. Due to the growth of the Company during 2003, the Company expects to meet this employment obligation during the second half of 2003.

On March 4, 2003, the Company completed a short-term financing to help it meet certain working capital needs as the Company was growing rapidly. The three-month, $500 note, which

accrued interest at 7.5% per annum, was converted into 125,000 shares of common stock at $4.00 per share on June 4, 2003, at the option of the note holder.

On March 25, 2003, the Company's primary lending bank agreed to amend the Company's credit facility. Among other things, this amendment included an extension of the credit agreement through June 30, 2004, a release of accounts receivable at the Company's U.K. subsidiary in order to allow that subsidiary to obtain its own revolving credit facility with a U.K. bank, and a formula adjustment in the borrowing base that enhanced the eligible receivables related to the U.S. military in recognition of the increasing business with the U.S. Army. As a result of the extension of this credit facility, the Company has classified the portion of this debt that is due and payable beyond one year as a long-term liability on the June 28, 2003 and the December 31, 2002 Consolidated Balance Sheets.

On April 29, 2003, Ultralife Batteries (UK) Ltd., the Company's wholly-owned U.K. subsidiary, completed an agreement for a revolving credit facility with a commercial bank in the U.K. Any borrowings against this credit facility are collateralized with that company's outstanding accounts receivable balances. The maximum credit available to that company under the facility is approximately $700. This credit facility provides the Company's U.K. operation with additional financing flexibility for its working capital needs. At June 28, 2003, the outstanding borrowings under this revolver were $586.

9. INCOME TAXES

The liability method, prescribed by SFAS No. 109, "Accounting for Income Taxes", is used in accounting for income taxes. Under this method, deferred tax assets and liabilities are determined based on differences between financial reporting and tax bases of assets and liabilities and are measured using the enacted tax rates and laws that may be in effect when the differences are expected to reverse. The Company recorded no income tax benefit or expense relating to the operating results generated during the six-month periods ended June 28, 2003 and June 30, 2002, as such income tax benefit or expense was offset by changes in the valuation allowance. A valuation allowance is required when it is more likely than not that the recorded value of a deferred tax asset will not be realized.

10. COMMITMENTS AND CONTINGENCIES

As of June 28, 2003, the Company had $50 in restricted cash in support of a corporate credit card account.

In March 1998, the Company received a $500 grant from the Empire State Development Corporation to fund certain equipment purchases. The grant was contingent upon the Company achieving and maintaining minimum employment levels for a period of five years. If annual levels of employment were not maintained, a portion of the grant might have become repayable. Through the first four years of the grant period, the Company met the requirements. The Company believes that it has also met the requirements in the fifth and final year, and it has recognized this portion of the grant into income. However, there is some uncertainty with the interpretation of the grant agreement, and it is possible that the Company may be required to repay $100 of the grant. The Company believes that the likelihood of a repayment is remote, and it is discussing its position with the Empire State Development Corporation accordingly. At June 28, 2003, there is no balance pertaining to this grant on the balance sheet.

The Company estimates future costs associated with expected product failure rates, material usage and service costs in the development of its warranty obligations. Warranty reserves are based on historical experience of warranty claims and generally will be estimated as a percentage of sales over the warranty period. In the event the actual results of these items differ from the estimates, an adjustment to the warranty obligation would be recorded. Changes in the Company's product warranty liability during the first six months of 2003 were as follows:

| | |
|---|---|
| Balance at December 31, 2002 | $236 |
| Accruals for warranties issued | 63 |
| Settlements made | (33) |
| Balance at June 28, 2003 | $266 |

The Company is subject to legal proceedings and claims which arise in the normal course of business. The Company believes that the final disposition of such matters will not have a material adverse effect on the financial position or results of operations of the Company.

In August 1998, the Company, its Directors, and certain underwriters were named as defendants in a complaint filed in the United States District Court for the District of New Jersey by certain shareholders, purportedly on behalf of a class of shareholders, alleging that the defendants, during the period April 30, 1998 through June 12, 1998, violated various provisions of the federal securities laws in connection with an offering of 2,500,000 shares of the Company's Common Stock. The complaint alleged that the Company's offering documents were materially incomplete, and as a result misleading, and that the purported class members purchased the Company's Common Stock at artificially inflated prices and were damaged thereby. Upon a motion made on behalf of the Company, the Court dismissed the shareholder action, without prejudice, allowing the complaint to be refiled. The shareholder action was subsequently refiled, asserting substantially the same claims as in the prior pleading. The Company again moved to dismiss the complaint. By Opinion and Order dated September 28, 2000, the Court dismissed the action, this time with prejudice, thereby barring plaintiffs from any further amendments to their complaint and directing that the case be closed. Plaintiffs filed a Notice of Appeal to the Third Circuit Court of Appeals and the parties submitted their briefs. Subsequently, the parties notified the Court of Appeals that they had reached an agreement in principle to resolve the outstanding appeal and settle the case upon terms and conditions which require submission to the District Court for approval. Upon application of the parties and in order to facilitate the parties' pursuit of settlement, the Court of Appeals issued an Order dated May 18, 2001 adjourning oral argument on the appeal and remanding the case to the District Court for further proceedings in connection with the proposed settlement.

Subsequent to the parties entering into the settlement agreement, the Company's insurance carrier commenced liquidation proceedings. The insurance carrier informed the Company that in light of the liquidation proceedings, it would no longer fund the settlement. In addition, the value of the insurance policy is in serious doubt. In April 2002, the Company and the insurance carrier for the underwriters offered to proceed with the settlement. Plaintiffs' counsel accepted the terms of the proposed settlement, amounting to $175 for the Company, which was previously accrued. The settlement has been approved by the Court and by the shareholders comprising the class, and the Company paid the settlement in June of 2003.

This matter is now completed and the Company will not incur any further expenses with regard to this lawsuit.

In conjunction with the Company's purchase/lease of its Newark, New York facility in 1998, the Company entered into a payment-in-lieu of tax agreement which provides the Company with real estate tax concessions upon meeting certain conditions. In connection with this agreement, a consulting firm performed a Phase I and II Environmental Site Assessment which revealed the existence of contaminated soil and ground water around one of the buildings. The Company retained an engineering firm which estimated that the cost of remediation should be in the range of $230. This cost, however, is merely an estimate and the cost may in fact be much higher. In February, 1998, the Company entered into an agreement with a third party which provides that the Company and this third party will retain an environmental consulting firm to conduct a supplemental Phase II investigation to verify the existence of the contaminants and further delineate the nature of the environmental concern. The third party agreed to reimburse the Company for fifty percent (50%) of the cost of correcting the environmental concern on the Newark property. The Company has fully reserved for its portion of the estimated liability. Test sampling was completed in the spring of 2001, and the engineering report was submitted to the New York State Department of Environmental Conservation (NYSDEC) for review. NYSDEC reviewed the report and, in January 2002, recommended additional testing. The Company responded by submitting a work plan to NYSDEC, which was approved in April 2002. The Company has sought proposals from engineering firms to complete the remedial work contained in the work plan, but it is unknown at this time whether the final cost to remediate will be in the range of the original estimate, given the passage of time. Because this is a voluntary remediation, there is no requirement for the Company to complete the project within any specific time frame. The ultimate resolution of this matter may have a significant adverse impact on the results of operations in the period in which it is resolved. Furthermore, the Company may face claims resulting in substantial liability which could have a material adverse effect on the Company's business, financial condition and the results of operations in the period in which such claims are resolved.

A retail end-user of a product manufactured by one of Ultralife's customers (the "Customer"), has made a claim against the Customer wherein it is asserted that the Customer's product, which is powered by an Ultralife battery, does not operate according to the Customer's product specification. No claim has been filed against Ultralife. However, in the interest of fostering good customer relations, in September 2002, Ultralife has agreed to lend technical support to the Customer in defense of its claim. Additionally, Ultralife will honor its warranty by replacing any batteries that may be determined to be defective. In the event a claim is filed against Ultralife and it is ultimately determined that Ultralife's product was defective, replacement of batteries to this Customer or end-user may have a material adverse effect on the Company's financial position and results of operations.

## 11. BUSINESS SEGMENT INFORMATION

The Company reports its results in four operating segments: Primary Batteries, Rechargeable Batteries, Technology Contracts and Corporate. The Primary Batteries segment includes 9-volt, cylindrical and various other non-rechargeable specialty batteries. The Rechargeable Batteries segment includes the Company's lithium polymer and lithium ion rechargeable batteries. The Technology Contracts segment includes revenues and related costs associated with various government and military development contracts. The Corporate segment consists of all other items that do not specifically relate to the three other segments and are not considered in the performance of the other segments.

Effective January 1, 2003, the Company revised its definition of segment contribution for each of its segments to be defined as gross margin (excluding the Corporate segment). Previously, segment contribution included applicable research and development costs. The Corporate segment now includes all of the Company's operating expenses, including research and development costs. This change in presentation was made to be consistent with the manner in which the Company's management views its

results from operations. Certain amounts in the prior year's segment information have been reclassified to conform to the current year presentation.

Three Months Ended June 28, 2003

| | Primary Batteries | Rechargeable Batteries | Technology Contracts | Corporate | Total |
|---|---|---|---|---|---|
| Revenues | $19,570 | $258 | $282 | $ -- | $ 20,110 |
| Segment contribution | 5,008 | (389) | 112 | (2,833) | 1,898 |
| Interest expense, net | | | | (146) | (146) |
| Equity loss in UTI | | | | -- | -- |
| Miscellaneous | | | | 397 | 397 |
| Income taxes | | | | -- | -- |
| Net income (loss) | | | | | $ 2,149 |
| Total assets | $31,956 | $3,249 | $140 | $ 6,191 | $ 41,536 |

Three Months Ended June 30, 2002

| | Primary Batteries | Rechargeable Batteries | Technology Contracts | Corporate | Total |
|---|---|---|---|---|---|
| Revenues | $ 8,299 | $ 71 | $208 | $ -- | $ 8,578 |
| Segment contribution | 1,562 | (497) | 20 | (17,172) | (16,087) |
| Interest expense, net | | | | (103) | (103) |
| Equity loss in UTI | | | | (678) | (678) |
| Miscellaneous | | | | 362 | 362 |
| Income taxes | | | | -- | -- |
| Net income (loss) | | | | | $(16,506) |
| Total assets | $21,351 | $4,256 | $ 33 | $ 8,681 | $ 34,321 |

Six Months Ended June 28, 2003

| | Primary Batteries | Rechargeable Batteries | Technology Contracts | Corporate | Total |
|---|---|---|---|---|---|
| Revenues | $34,202 | $ 638 | $698 | $ -- | $ 35,538 |
| Segment contribution | 8,172 | (596) | 314 | (5,380) | 2,510 |
| Interest expense, net | | | | (237) | (237) |
| Equity loss in UTI | | | | -- | -- |
| Miscellaneous | | | | 187 | 187 |
| Income taxes | | | | -- | -- |
| Net income (loss) | | | | | $ 2,460 |
| Total assets | $31,956 | $3,249 | $140 | $ 6,191 | $ 41,536 |

Six Months Ended June 30, 2002

| | Primary Batteries | Rechargeable Batteries | Technology Contracts | Corporate | Total |
|---|---|---|---|---|---|
| Revenues | $17,039 | $ 158 | $243 | $ -- | $ 17,440 |
| Segment contribution | 3,003 | (1,018) | 22 | (20,191) | (18,184) |
| Interest expense, net | | | | (201) | (201) |
| Equity loss in UTI | | | | (1,179) | (1,179) |
| Miscellaneous | | | | 265 | 265 |
| Income taxes | | | | -- | -- |
| Net income (loss) | | | | | $(19,299) |
| Total assets | $21,351 | $ 4,256 | $ 33 | $ 8,681 | $ 34,321 |

12. RECENT ACCOUNTING PRONOUNCEMENTS

In November 2002, the Financial Accounting Standards Board ("FASB") issued Interpretation No. 45, "Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Others Indebtedness." This Interpretation elaborates on the disclosures to be made by a guarantor in its interim and annual financial statements about its obligations under certain guarantees that it has issued. It also clarifies that a guarantor is required to recognize, at the inception of a guarantee, a liability for the fair value of the obligation undertaken in issuing the guarantee. This Interpretation also incorporates, without change, the guidance in FASB Interpretation No. 34, "Disclosure of Indirect Guarantees of Indebtedness of Others." The initial recognition and measurement provisions of this Interpretation are applicable on a prospective basis to guarantees issued or modified after December 31, 2002, irrespective of the guarantor's fiscal year-end. The disclosure requirements in this Interpretation are effective for financial statements of interim or annual periods ending after December 15, 2002. The only material guarantees that the Company has in accordance with FASB Interpretation No. 45 are product warranties. All such guarantees have been appropriately recorded in the financial statements.

In December 2002, the FASB issued Statement of Financial Accounting Standards ("SFAS") No. 148, "Accounting for Stock-Based Compensation-Transition and Disclosure-an amendment of FASB Statement No. 123." This statement amends SFAS No. 123, "Accounting for Stock-Based Compensation," to provide alternative methods of transition for a voluntary change to the fair value based method of accounting for stock-based employee compensation. In addition, this Statement amends the disclosure requirements of SFAS No. 123 to require prominent disclosures in both annual and interim financial statements about the method of accounting for stock-based employee compensation and the effect of the method used on reported results. SFAS No. 148 does not permit the use of the original SFAS No. 123 prospective method of transition for changes to the fair value based method made in fiscal years after December 15, 2003. The Company currently applies the intrinsic value method and has no plans to convert to the fair value method.

In December 2002, the FASB issued Interpretation No. 46 "Consolidation of Variable Interest Entities." This Interpretation requires companies to reevaluate their accounting for certain investments in "variable interest entities." A variable interest entity is a corporation, partnership, trust, or any other legal structure used for business purposes that either (a) does not have equity investors with voting rights or (b) has equity investors that do not provide sufficient financial resources for the entity to support its activities. A variable interest entity often holds financial assets, including loans or receivables, real estate or other property. A variable interest entity may be essentially passive or it may engage in research and development or other activities on behalf of another company. Variable interest entities are to be consolidated if the Company is subject to a majority of the risk of loss from the variable interest entity's activities or entitled to receive a majority of the entity's residual returns or both. The disclosure requirements of this Interpretation are effective for all financial statements issued after January 31, 2003. The consolidation requirements of this Interpretation are effective for all periods beginning after June 15, 2003. The Company has no investments in variable interest entities.

In April 2003, the FASB issued SFAS No. 149, "Amendment of Statement 133 on Derivative Instruments and Hedging Activities." The standard amends and clarifies financial reporting for derivative instruments and for hedging activities accounted for under SFAS No. 133 and is effective for contracts entered into or modified, and for hedges designated, after June 30, 2003. The Company has

no derivative instruments and adoption of the standard is not expected to have a material impact on the Company's consolidated financial position, results of operations or cash flows.

In May 2003, the FASB issued SFAS No. 150, "Accounting for Certain Instruments with Characteristics of Both Liabilities and Equity." The standard establishes how an issuer classifies and measures certain freestanding financial instruments with characteristics of liabilities and equity and requires that such instruments be classified as liabilities. The standard is effective for financial instruments entered into or modified after May 31, 2003 and is otherwise effective at the beginning of the first interim period beginning after June 15, 2003. Adoption of the standard is not expected to have a material impact on the Company's consolidated financial position, results of operations or cash flows.

Item 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (in whole dollars)

The Private Securities Litigation Reform Act of 1995 provides a "safe harbor" for forward-looking statements. This report contains certain forward-looking statements and information that are based on the beliefs of management as well as assumptions made by and information currently available to management. The statements contained in this report relating to matters that are not historical facts are forward-looking statements that involve risks and uncertainties, including, but not limited to, future demand for the Company's products and services, the successful commercialization of the Company's advanced rechargeable batteries, general economic conditions, government and environmental regulation, competition and customer strategies, technological innovations in the primary and rechargeable battery industries, changes in the Company's business strategy or development plans, capital deployment, business disruptions, including those caused by fires, raw materials supplies, environmental regulations, and other risks and uncertainties, certain of which are beyond the Company's control. Should one or more of these risks or uncertainties materialize, or should underlying assumptions prove incorrect, actual results may differ materially from those described herein as anticipated, believed, estimated or expected.

This Management's Discussion and Analysis of Financial Condition and Results of Operations should be read in conjunction with the accompanying consolidated financial statements and notes thereto contained herein and the Company's consolidated financial statements and notes thereto contained in the Company's Transition Report on Form 10-K as of and for the six-month period ended December 31, 2002.

General

Ultralife Batteries, Inc. develops, manufactures and markets a wide range of standard and customized lithium primary (non-rechargeable), lithium ion and lithium polymer rechargeable batteries for use in a wide array of applications. The Company believes that its technologies allow the Company to offer batteries that are flexibly configured, lightweight and generally achieve longer operating time than many competing batteries currently available. The Company has focused on manufacturing a family of lithium primary batteries for military, industrial and consumer applications, which it believes is one of the most comprehensive lines of lithium manganese dioxide primary batteries commercially available. The Company also supplies rechargeable lithium ion and lithium polymer batteries for use in portable electronic applications.

Effective December 31, 2002, the Company changed its fiscal year-end from June 30 to December 31.

For several years, the Company had incurred net operating losses primarily as a result of funding research and development activities and, to a lesser extent, incurring manufacturing and selling, general and administrative costs. During the twelve month period ended June 30, 2002, the Company realigned its resources to bring costs more in line with revenues, moving the Company closer to achieving operating cash breakeven and profitability. In addition, the Company refined its rechargeable strategy to allow it to be more effective in the marketplace. As a result of the Company's focus on its key financial goals, the Company successfully achieved operating profitability for the first time in its history in the quarter ended March 29, 2003.

The Company reports its results in four operating segments: Primary Batteries, Rechargeable Batteries, Technology Contracts and Corporate. The Primary Batteries segment includes 9-volt, cylindrical and various other non-rechargeable specialty batteries. The Rechargeable Batteries segment includes the Company's lithium polymer and lithium ion rechargeable batteries. The Technology Contracts segment includes revenues and related costs associated with various government and military

development contracts. The Corporate segment consists of all other items that do not specifically relate to the three other segments and are not considered in the performance of the other segments.

## Results of Operations

Three months ended June 28, 2003 and June 30, 2002

Revenues. Consolidated revenues reached a quarterly record of $20,110,000 for the three-month period ended June 28, 2003, an increase of $11,532,000, or 134%, from the $8,578,000 reported in the same quarter in the prior year. Primary battery sales increased $11,271,000, or 136%, from $8,299,000 last year to $19,570,000 this year, mainly as a result of strong shipments of HiRate(R) battery products, including sales of BA-5390 batteries used mainly in various communications and weapons applications in the military. Rechargeable revenues rose $187,000 to $258,000 as the Company's broadened strategy to include battery assemblies resulted in new customers. Technology Contract revenues increased $74,000 to $282,000 in the second quarter of 2003 as certain milestones were met on a development contract with the U.S. Army.

Cost of Products Sold. Cost of products sold totaled $15,379,000 for the quarter ended June 28, 2003, an increase of $7,886,000, or 105% over the same three-month period a year ago. The gross margin on consolidated revenues for the quarter was $4,731,000, or 24% of revenues, an improvement of $3,646,000 over the $1,085,000, or 13% of revenues, in the same quarter in the prior year. Gross margins in the Company's primary battery operations improved $3,446,000, from $1,562,000 in 2002 to $5,008,000 in 2003. As a percentage of revenues, primary battery margins amounted to 26% in the second quarter of 2003 compared with 19% in 2002. This improvement resulted mainly from higher sales and production volumes that spread manufacturing overhead costs over a broader base, as well as improvements in manufacturing efficiencies. In the Company's rechargeable operations, the gross margin loss amounted to $389,000 in the second quarter of 2003 compared with $497,000 in the same period in 2002. This improvement in the rechargeable area was the result of higher sales volumes and the favorable impact from cost savings initiatives that were implemented during the first quarter in 2002, as well as lower depreciation charges. Gross margins in the Technology Contract segment increased from $20,000 in 2002 to $112,000 in 2003 as a result of higher sales.

During the second quarter of 2003, the Company's production volumes continued to increase in order to keep pace with product demand. As a result, the Company increased its direct labor force by more than 130 people, or approximately 25% since March 2003. Certain inefficiencies in the production operation that resulted from the rapid manufacturing ramp-up, including the need to work significant amounts of overtime to meet customer delivery requirements, are expected to improve as the direct labor force stabilizes and additional production equipment is installed to alleviate various manual processes. In addition, the Company expects to realize further direct material cost reductions over the levels achieved in the first half of 2003 as production volumes increase.

Operating Expenses. Operating expenses for the three months ended June 28, 2003 totaled $2,833,000, quite consistent with the prior year's amount of $2,854,000, excluding the $14,318,000 impairment charge related to rechargeable assets. While research and development costs declined $453,000 as the development efforts for rechargeable products were diminished and depreciation expenses declined, selling, general and administrative expenses increased $432,000 between the two periods due to higher compensation expenses and higher professional fees. Overall, operating expenses as a percentage of sales improved significantly, from 33% in the June 2002 quarter to 14% in the June 2003 quarter, as the revenue base increased significantly.

Other Income (Expense). Interest expense, net, for the second quarter of 2003 was $146,000, an increase of $43,000 from the comparable period in 2002, due mainly as a result of interest expense

associated with the $500,000 short-term note that was issued in March 2003. Equity loss in Ultralife Taiwan, Inc., (UTI) was $678,000 in the second quarter of 2002 compared with zero in the second quarter of 2003. This change resulted mainly from an October 2002 change in the method of accounting for the Company's investment in UTI, from the equity method of accounting to the cost method of accounting. In October 2002, the Company sold a portion of its equity investment in UTI, reducing its ownership interest from approximately 30% to approximately 10.6%. Subsequent to the completion of this transaction, UTI has raised additional equity capital and the Company's ownership interest in UTI has declined to approximately 9.2% as of June 28, 2003. Miscellaneous income rose from $362,000 in 2002 to $397,000 in 2003. This change related primarily to higher gains on foreign currency transactions, mainly due to changes between the British pound sterling and the U.S. dollar. More specifically, the Company has had intercompany transactions over the years with its wholly-owned U.K. subsidiary, Ultralife Batteries (UK) Ltd., that have resulted in a net payable balance to the U.S. parent company, denominated in U.S. dollars. While there was no cash impact to the Company as a result of the translation of these intercompany balances during the periods presented, foreign currency translation losses were recognized as the British pound sterling strengthened against the U.S. dollar during each of the three-month periods ended June 28, 2003 and June 30, 2002.

Net Income. Net income and diluted earnings per share were $2,149,000 and $0.16, respectively, for the three months ended June 28, 2003, compared to a net loss and loss per share of $16,506,000 and $1.28, respectively, for the same quarter last year, primarily as a result of the reasons described above. Average common shares outstanding increased mainly due to the Company's private equity offering in April 2002, stock option exercises in 2003, and the conversion of a short-term note in June 2003, offset in part by the reacquisition of shares from UTI that resulted from the Company's sale of a portion of its interest in UTI in October 2002. The increase in the Company's stock price during 2003 had a greater dilutive effect on the average diluted shares outstanding computation compared with the same period in 2002.

Six months ended June 28, 2003 and June 30, 2002

Revenues. Consolidated revenues totaled $35,538,000 for the six-month period ended June 28, 2003, an increase of $18,098,000, or 104%, from the $17,440,000 reported in the same quarter in the prior year. Primary battery sales increased $17,163,000, or 101%, from $17,039,000 last year to $34,202,000 this year, mainly as a result of strong shipments of HiRate(R) battery products, including sales of BA-5390 batteries used mainly in various communications and weapons applications in the military, as well as higher 9-volt sales. Rechargeable revenues rose $480,000 to $638,000 as the Company's broadened strategy including battery assemblies began to develop new customers. Technology Contract revenues increased $455,000 to $698,000 in the first six months of 2003 as certain milestones were met on a development contract with the U.S. Army.

Cost of Products Sold. Cost of products sold totaled $27,648,000 for the first half of 2003, an increase of $12,215,000, or 79% over the same six-month period a year ago. The gross margin on consolidated revenues for the first six months of 2003 was $7,890,000, or 22% of revenues, an improvement of $5,883,000 over the $2,007,000, or 12% of revenues, in the same period in the prior year. Gross margins in the Company's primary battery operations improved $5,169,000, from $3,003,000 in 2002 to $8,172,000 in 2003. As a percentage of revenues, primary battery margins amounted to 24% in the first half of 2003 compared with 18% in 2002. This improvement resulted mainly from higher sales and production volumes, in addition to manufacturing efficiencies. In the Company's rechargeable operations, the gross margin loss amounted to $596,000 in the first six months of 2003 compared with a loss of $1,018,000 in the same period in 2002. This improvement in the rechargeable area was the result of higher sales volumes and the favorable impact from cost savings initiatives that were implemented during the first quarter in 2002, as well as lower depreciation charges. Gross margins in the Technology Contract segment increased from $22,000 in 2002 to $314,000 in 2003 as a result of higher sales.

During the first half of 2003, the Company's production volumes increased in order to keep pace with product demand. As a result, the Company increased its direct labor force by more than 300 people, or approximately 80% since December 2002. Certain inefficiencies in the production operation resulting from the rapid manufacturing ramp-up, including the need to work significant amounts of overtime to meet customer delivery requirements, are expected to improve as the direct labor force stabilizes and additional production equipment is installed to alleviate various manual processes. In addition, the Company expects to realize further direct material cost reductions over the levels achieved in the first half of 2003 as production volumes increase.

Operating Expenses. Operating expenses for the six months ended June 28, 2003 totaled $5,380,000, a decrease of $493,000 from the prior year, excluding the $14,318,000 impairment charge related to rechargeable assets. This decrease was primarily attributable to lower research and development costs, which declined $906,000, as the development efforts for rechargeable products were diminished and depreciation expenses declined. Selling, general and administrative expenses increased $413,000 to $4,149,000 in 2003, mainly as a result of higher compensation expenses and higher professional fees. As a percentage of sales, total operating expenses (excluding impairment charges) declined noticeably from 34% in the first six months of 2002 to 15% in the same period in 2003, mostly due to the higher revenue base.

Other Income (Expense). Interest expense, net, for the first six months of 2003 rose $36,000 to $237,000 in the first six months of 2003, primarily due to interest expense associated with the $500,000 short-term convertible note that was issued in March 2003. Equity loss in Ultralife Taiwan, Inc., (UTI) was $1,179,000 in the first half of 2002 compared with zero in the first half of 2003. This change resulted mainly from an October 2002 change in the method of accounting for the Company's investment in UTI, from the equity method of accounting to the cost method of accounting. In October 2002, the Company sold a portion of its equity investment in UTI, reducing its ownership interest from approximately 30% to approximately 10.6%. Subsequent to the completion of this transaction, UTI has raised additional equity capital and the Company's ownership interest in UTI has declined to approximately 9.2% as of June 28, 2003. Miscellaneous income declined from $265,000 in 2002 to $187,000 in 2003, due to lower gains from the impact of foreign currency translations. These foreign currency gains relate mainly to changes between the British pound sterling and the U.S. dollar. More specifically, the Company has had intercompany transactions over the years with its wholly-owned U.K. subsidiary, Ultralife Batteries (UK) Ltd., that have resulted in a net payable balance to the U.S. parent company, denominated in U.S. dollars. While there was no cash impact to the Company as a result of the translation of these intercompany balances during the periods presented, foreign currency translation gains were recognized as the British pound sterling strengthened against the U.S. dollar during each of the six-month periods ended June 28, 2003 and June 30, 2002.

Net Income. Net income and diluted earnings per share were $2,460,000 and $0.19, respectively, for the six months ended June 28, 2003, compared to a net loss and loss per share of $19,299,000 and $1.49, respectively, for the same six-month period last year, primarily as a result of the reasons described above. Average common shares outstanding changed due to the Company's private equity offering in April 2002, stock option exercises during the first half of 2003, and the conversion of a short-term note in June 2003, offset in part by the reacquisition of shares from UTI that resulted from the Company's sale of a portion of its interest in UTI in October 2002. The increase in the Company's stock price during 2003 had a greater dilutive effect on the average diluted shares outstanding computation compared with the same period in 2002.

## Liquidity and Capital Resources

As of June 28, 2003, cash equivalents and available for sale securities totaled $1,614,000, excluding restricted cash of $50,000. During the six months ended June 28, 2003, the Company used $243,000 of cash in operating activities as compared to $2,930,000 for the six months ended June 30, 2002. During the first six months of 2003, the Company's net income plus depreciation and amortization were offset by an increase in working capital usage, particularly an increase in accounts receivable related to the significant rise in sales during the period. In the six months ended June 28, 2003, the Company used $3,278,000 to purchase plant, property and equipment, an increase of $2,486,000 from the prior year's capital expenditures, mainly as a result of the need to increase production capacity for cylindrical cells as demand from military customers grew significantly. During the six month period ended June 28, 2003, the Company generated $3,784,000 in funds from financing activities. The financing activities included inflows from issuance of stock, mainly as stock options were exercised during the period, a $500,000 90-day note converted into shares of common stock in June 2003, and the final payment of $117,000 that was received on a $750,000 government grant/loan, offset in part by payments on debt obligations. In addition, the Company had accessed $2,440,000 of its revolving credit facilities as of June 28, 2003 to finance working capital needs.

Months cost of sales in inventory at June 28, 2003 was 1.7 months based on a rolling three-month average, compared with 2.0 months at December 31, 2002. This metric is indicative of the rapid turnaround of product to the military and the high volume of sales during the first half of 2003, as well as the Company's continuing focus to improve purchasing procedures and inventory controls. The Company's Days Sales Outstanding (DSOs) was an average of 46 days for the first half of 2003, compared with an average of 60 days for the same six-month period in 2002. This improvement in DSOs mainly reflects the significant increase in sales to the U.S. military and the associated favorable impact from the timely payments made by them.

At June 28, 2003, the Company had a capital lease obligation outstanding of $103,000 for the Company's Newark, New York offices and manufacturing facilities.

As of June 28, 2003, the Company had open capital commitments to purchase approximately $840,000 of production machinery and equipment.

On March 25, 2003, the Company's primary lending bank and the Company agreed to amend the Company's $15,000,000 credit facility. Among other things, the amendment extended the maturity date to June 30, 2004, allowed for the collateral release of accounts receivable related to the Company's subsidiary in the U.K. affording it the ability to enter into a separate revolving credit facility, and also revised certain limitations on customer concentration to account for the increased sales activity with the U.S. military. The Company has classified the portion of this debt that is due and payable beyond one year as a long-term liability on the June 28, 2003 and December 31, 2002 Consolidated Balance Sheets. As of June 28, 2003, the Company had $1,667,000 outstanding under the term loan component of its $15,000,000 credit facility, and had $1,853,000 of borrowings outstanding under the revolver component of the credit facility. The Company's additional borrowing capacity under the revolver component of the credit facility as of June 28, 2003 was approximately $4,000,000, net of outstanding letters of credit of $3,800,000. At June 28, 2003, the Company's net worth was $26,292,000, compared to the debt covenant requiring a minimum net worth of approximately $19,200,000.

On April 29, 2003, Ultralife Batteries (UK) Ltd., the Company's wholly-owned U.K. subsidiary, completed an agreement for a revolving credit facility with a commercial bank in the U.K. Any borrowings against this credit facility are collateralized with that company's outstanding accounts receivable balances. The maximum credit available to that company under the facility is approximately $700,000. This credit facility provides the Company's U.K. operation with additional financing flexibility for its working capital needs. At June 28, 2003, the outstanding borrowings under this revolver were $586,000.

In November 2001, the Company received approval for a $750,000 grant/loan from a federally sponsored small cities program. The grant/loan has assisted in funding capital expansion plans that the Company expects will lead to job creation. The Company has been reimbursed for approved capital as it incurred the cost. In August 2002, the $750,000 small cities grant/loan documentation was finalized and the Company was reimbursed approximately $400,000 for costs it had incurred to date for equipment purchases applicable under this grant/loan. By the end of March 2003, all $750,000 had been advanced to the Company. During the first quarter of 2003, $117,000 under this grant/loan was reimbursed as the Company incurred additional expenses and submitted requests for reimbursement. If the Company meets its employment quota requirements by April 1, 2005, the loan and all associated accrued interest will be forgiven. If the Company does not meet its employment quota requirements, then the funds advanced and the associated interest will be converted into a loan that will be repaid over a seven-year period. The Company has initially recorded the proceeds from this grant/loan as a long-term liability and will record these proceeds as income as the certainty of meeting the employment criteria become definitive. Interest has been accrued at a rate of 5% per year. Due to the growth of the Company during 2003, the Company expects to meet this employment obligation during the second half of 2003.

On March 4, 2003, the Company completed a short-term financing to help it meet certain working capital needs as the Company was growing rapidly. Pursuant to the terms of the note, the three-month, $500,000 note, which accrued interest at 7.5% per annum, was converted into 125,000 shares of common stock at $4.00 per share on June 4, 2003. Accrued interest was paid to the noteholder on the maturity date.

During the first six months of 2003, the Company issued 169,025 shares of common stock as a result of exercises of stock options and warrants. The Company received approximately $1,100,000 in cash proceeds as a result of these transactions.

The Company is optimistic about its future prospects and growth potential. However, the recent rapid growth of the business has created a near-term need for certain machinery, equipment and working capital in order to increase capacity and build product to meet demand. In certain areas of manufacturing, the Company has been producing at or near capacity. In order to increase its capacity in these areas, the Company has added a significant number of people and is adding machinery and equipment in order to continue to fulfill this demand. The Company continues to explore other sources of capital, including utilizing its unleveraged assets as collateral for additional borrowing capacity, issuing debt and raising equity through a private or public offering. Although it is evaluating these alternatives, the Company believes it has the ability over the next 12 months to finance its operations primarily through internally generated funds, or through the use of additional financing that currently is available to the Company.

As described in Part II, Item 1, "Legal Proceedings", the Company is involved in certain environmental matters with respect to its facility in Newark, New York. Although the Company has reserved for expenses related to this, there can be no assurance that this will be the maximum amount. The ultimate resolution of this matter may have a significant adverse impact on the results of operations in the period in which it is resolved.

The Company typically offers warranties against any defects due to product malfunction or workmanship for a period up to one year from the date of purchase. The Company also offers a 10-year warranty on its 9-volt batteries that are used in ionization-type smoke detector applications. The Company provides for a reserve for this potential warranty expense, which is based on an analysis of historical warranty issues. There is no assurance that future warranty claims will be consistent with past history, and in the event the Company's experiences a significant increase in warranty claims, there is no assurance that the Company's reserves are sufficient. This could have a material adverse effect on the Company's business, financial condition and results of operations.

Outlook

The Company expects revenues in its third quarter of calendar 2003 to reach at least $20,000,000. Demand for the BA-5390 battery remains very strong, and the Company continues to respond as quickly as possible to the orders on hand. The Company believes that the order activity from the military will continue to be strong throughout the remainder of 2003 and that it is likely to continue into 2004. In support of this, on August 5, 2003, the Company announced that it had been awarded its largest contract to date for its BA-5390/U battery valued at up to $28,000,000, by the U.S. Army Communications Electronics Command (CECOM). Shipments are scheduled to begin in November 2003 and continue into the first half of 2004, subject to negotiated delivery requirements. In addition to the strong demand from the military, orders from commercial customers for 9-volts and other batteries remain strong. Sampling and design activity for various rechargeable products remains high, although the Company is conservatively projecting modest revenues in this part of the business for the remainder of 2003.

Looking ahead for the full calendar year of 2003, the Company remains optimistic about its sales prospects and the status of the manufacturing operations. At this time, the Company is now projecting revenues of approximately $75,000,000 (up from the previous guidance of at least $65,000,000), an approximately 125% increase over the $33,039,000 reported for the comparable 12 months in the period ended December 31, 2002. The Company is raising its outlook due to the strong order activity it has experienced recently, particularly from the military, and its success in ramping up production to meet demand.

The Company has a fairly substantial fixed cost infrastructure to support its overall operations. The Company believes that incremental sales volumes will generate added gross margins in the range of 30% to 50%. Conversely, decreasing sales volumes will result in the opposite effect. During the December 2001 and March 2002 quarters, the Company was able to significantly reduce costs through various cost savings actions, moving it toward cash generation and profitability. As the Company continues to grow and leverage this infrastructure, it believes that sustainable profitability can be achieved. The Company believes that consistent, quarterly revenues in the range of $11,000,000 to $12,000,000, depending on mix, is the operating income breakeven point for profitability.

The Company continues to monitor its operating costs very tightly. Over the remainder of the calendar year, the Company is projecting operating expenses to be in line with or modestly higher than the first two quarters of 2003.

The Company expects that operating income in the September 2003 quarter will exceed $2,100,000, based on the Company's projected revenues and improving manufacturing efficiencies. This compares to an operating loss of $1,917,000 in the September 2002 quarter. For the full year of 2003, the Company is projecting that operating income will be at least $7,000,000, based on a continuing strong demand for the Company's products, compared with an operating loss of $21,838,000, including a $14,318,000 asset impairment charge, for the full calendar year of 2002. The guidance previously provided called for basic earnings per share in the range of $0.35 to $0.45 and revenue of $65,000,000, which suggested operating income in the range of approximately $5,000,000 to $6,300,000.

In order to meet the significant demand from the military, the Company expects to continue to make prudent investments in capital equipment that have a very short payback. At this time, the Company believes that expenditures for capital projects during 2003 will be approximately $5,000,000, based on the recent volume of orders and the expectation that demand will continue to increase across all product lines. Since the lead time for ordering certain production equipment can range from six to twelve months, the Company must make some up front investments in capital in order to increase its capacity to meet anticipated demand. The recent success and the continued outlook for growth is requiring the Company to make some such investments in new equipment during 2003. The Company carefully

evaluates such projects and will only make capital investments when necessary and when there is typically a favorable payback period.

As the Company's volume grows, it expects that working capital needs related to increasing sales volumes and inventory levels will be able to be financed by its revolving credit facility. The Company continually explores its financing alternatives, including utilizing its unleveraged assets as collateral for additional borrowing capacity, refinancing current debt or issuing new debt, and raising equity through a private or public offering. Although it is evaluating these alternatives, the Company believes it has the ability over the next 12 months to finance its operations primarily through internally generated funds, or through the use of additional financing that currently is available to the Company. While the Company is confident that it will be successful in continuing to arrange adequate financing to support its growth, there can be no assurance that the Company will be able to do so. Therefore, this could have a material adverse effect on the Company's business, financial position and results of operations.

New Accounting Pronouncements

In November 2002, the Financial Accounting Standards Board ("FASB") issued Interpretation No. 45, "Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Others Indebtedness." This Interpretation elaborates on the disclosures to be made by a guarantor in its interim and annual financial statements about its obligations under certain guarantees that it has issued. It also clarifies that a guarantor is required to recognize, at the inception of a guarantee, a liability for the fair value of the obligation undertaken in issuing the guarantee. This Interpretation also incorporates, without change, the guidance in FASB Interpretation No. 34, "Disclosure of Indirect Guarantees of Indebtedness of Others." The initial recognition and measurement provisions of this Interpretation are applicable on a prospective basis to guarantees issued or modified after December 31, 2002, irrespective of the guarantor's fiscal year-end. The disclosure requirements in this Interpretation are effective for financial statements of interim or annual periods ending after December 15, 2002. The only material guarantees that the Company has in accordance with FASB Interpretation No. 45 are product warranties. All such guarantees have been appropriately recorded in the financial statements.

In December 2002, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards ("SFAS") No. 148, "Accounting for Stock-Based Compensation-Transition and Disclosure-an amendment of FASB Statement No. 123." This statement amends SFAS No. 123, "Accounting for Stock-Based Compensation," to provide alternative methods of transition for a voluntary change to the fair value based method of accounting for stock-based employee compensation. In addition, this Statement amends the disclosure requirements of SFAS No. 123 to require prominent disclosures in both annual and interim financial statements about the method of accounting for stock-based employee compensation and the effect of the method used on reported results. SFAS No. 148 does not permit the use of the original SFAS No. 123 prospective method of transition for changes to the fair value based method made in fiscal years after December 15, 2003. The Company currently applies the intrinsic value method and has no plans to convert to the fair value method.

In December 2002, the FASB issued Interpretation No. 46 "Consolidation of Variable Interest Entities." This Interpretation requires companies to reevaluate their accounting for certain investments in "variable interest entities." A variable interest entity is a corporation, partnership, trust, or any other legal structure used for business purposes that either (a) does not have equity investors with voting rights or (b) has equity investors that do not provide sufficient financial resources for the entity to support its activities. A variable interest entity often holds financial assets, including loans or receivables, real estate or other property. A variable interest entity may be essentially passive or it may engage in research and development or other activities on behalf of another company. Variable interest entities are to be consolidated if the Company is subject to a majority of the risk of loss from the variable interest entity's activities or entitled to receive a majority of the entity's residual returns or both. The disclosure

requirements of this Interpretation are effective for all financial statements issued after January 31, 2003. The consolidation requirements of this Interpretation are effective for all periods beginning after June 15, 2003. The Company has no investments in variable interest entities.

In April 2003, the FASB issued SFAS No. 149, "Amendment of Statement 133 on Derivative Instruments and Hedging Activities." The standard amends and clarifies financial reporting for derivative instruments and for hedging activities accounted for under SFAS No. 133 and is effective for contracts entered into or modified, and for hedges designated, after June 30, 2003. The Company has no derivative instruments and adoption of the standard is not expected to have a material impact on the Company's consolidated financial position, results of operations or cash flows.

In May 2003, the FASB issued SFAS No. 150, "Accounting for Certain Instruments with Characteristics of Both Liabilities and Equity." The standard establishes how an issuer classifies and measures certain freestanding financial instruments with characteristics of liabilities and equity and requires that such instruments be classified as liabilities. The standard is effective for financial instruments entered into or modified after May 31, 2003 and is otherwise effective at the beginning of the first interim period beginning after June 15, 2003. Adoption of the standard is not expected to have a material impact on the Company's consolidated financial position, results of operations or cash flows.

## Item 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISKS

The Company is exposed to various market risks in the normal course of business, primarily interest rate risk and changes in market value of its investments and believes its exposure to these risks is minimal. The Company's investments are made in accordance with the Company's investment policy and primarily consist of commercial paper and U.S. corporate bonds. The Company does not currently invest in derivative financial instruments.

## Item 4. CONTROLS AND PROCEDURES

Within the 90 days prior to the date of this Form 10-Q, the Company carried out an evaluation, under the supervision and with the participation of the company's management, including the Company's president and chief executive officer, along with the Company's vice president - finance and chief financial officer, of the effectiveness of the design and operation of the Company's disclosure controls and procedures pursuant to Exchange Act 13a-14. Based upon that evaluation, the Company's president and chief executive officer, along with the Company's vice president - finance and chief financial officer, concluded that the Company's disclosure controls and procedures are effective in timely alerting them to material information related to the Company (including its consolidated subsidiaries) required to be included in the Company's periodic filings with the Securities and Exchange Commission. There have been no significant changes in the Company's internal controls or in other factors that could significantly affect internal controls subsequent to the date the Company carried out its evaluation.

PART II OTHER INFORMATION

Item 1. Legal Proceedings

The Company is subject to legal proceedings and claims which arise in the normal course of business. The Company believes that the final disposition of such matters will not have a material adverse effect on the financial position or results of operations of the Company.

In August 1998, the Company, its Directors, and certain underwriters were named as defendants in a complaint filed in the United States District Court for the District of New Jersey by certain shareholders, purportedly on behalf of a class of shareholders, alleging that the defendants, during the period April 30, 1998 through June 12, 1998, violated various provisions of the federal securities laws in connection with an offering of 2,500,000 shares of the Company's Common Stock. The complaint alleged that the Company's offering documents were materially incomplete, and as a result misleading, and that the purported class members purchased the Company's Common Stock at artificially inflated prices and were damaged thereby. Upon a motion made on behalf of the Company, the Court dismissed the shareholder action, without prejudice, allowing the complaint to be refiled. The shareholder action was subsequently refiled, asserting substantially the same claims as in the prior pleading. The Company again moved to dismiss the complaint. By Opinion and Order dated September 28, 2000, the Court dismissed the action, this time with prejudice, thereby barring plaintiffs from any further amendments to their complaint and directing that the case be closed. Plaintiffs filed a Notice of Appeal to the Third Circuit Court of Appeals and the parties submitted their briefs. Subsequently, the parties notified the Court of Appeals that they had reached an agreement in principle to resolve the outstanding appeal and settle the case upon terms and conditions which require submission to the District Court for approval. Upon application of the parties and in order to facilitate the parties' pursuit of settlement, the Court of Appeals issued an Order dated May 18, 2001 adjourning oral argument on the appeal and remanding the case to the District Court for further proceedings in connection with the proposed settlement.

Subsequent to the parties entering into the settlement agreement, the Company's insurance carrier commenced liquidation proceedings. The insurance carrier informed the Company that in light of the liquidation proceedings, it would no longer fund the settlement. In addition, the value of the insurance policy is in serious doubt. In April 2002, the Company and the insurance carrier for the underwriters offered to proceed with the settlement. Plaintiffs' counsel accepted the terms of the proposed settlement, amounting to $175,000 for the Company, which was previously accrued. . The settlement has been approved by the Court and by the shareholders comprising the class, and the Company paid the settlement in June of 2003.

This matter is now completed and the Company will not incur any further expenses with regard to this lawsuit.

In conjunction with the Company's purchase/lease of its Newark, New York facility in 1998, the Company entered into a payment-in-lieu of tax agreement which provides the Company with real estate tax concessions upon meeting certain conditions. In connection with this agreement, a consulting firm performed a Phase I and II Environmental Site Assessment which revealed the existence of contaminated soil and ground water around one of the buildings. The Company retained an engineering firm which estimated that the cost of remediation should be in the range of $230,000. This cost, however, is merely an estimate and the cost may in fact be much higher. In February, 1998, the Company entered into an agreement with a third party which provides that the Company and this third party will retain an environmental consulting firm to conduct a supplemental Phase II investigation to verify the existence of the contaminants and further delineate the nature of the environmental concern. The third party agreed to reimburse the Company for fifty percent (50%) of the cost of correcting the environmental concern on the Newark property. The Company has fully reserved for its portion of the estimated liability. Test

sampling was completed in the spring of 2001, and the engineering report was submitted to the New York State Department of Environmental Conservation (NYSDEC) for review. NYSDEC reviewed the report and, in January 2002, recommended additional testing. The Company responded by submitting a work plan to NYSDEC, which was approved in April 2002. The Company has sought proposals from engineering firms to complete the remedial work contained in the work plan, but it is unknown at this time whether the final cost to remediate will be in the range of the original estimate, given the passage of time. Because this is a voluntary remediation, there is no requirement for the Company to complete the project within any specific time frame. The ultimate resolution of this matter may have a significant adverse impact on the results of operations in the period in which it is resolved. Furthermore, the Company may face claims resulting in substantial liability which could have a material adverse effect on the Company's business, financial condition and the results of operations in the period in which such claims are resolved.

A retail end-user of a product manufactured by one of Ultralife's customers (the "Customer"), has made a claim against the Customer wherein it is asserted that the Customer's product, which is powered by an Ultralife battery, does not operate according to the Customer's product specification. No claim has been filed against Ultralife. However, in the interest of fostering good customer relations, in September 2002, Ultralife has agreed to lend technical support to the Customer in defense of its claim. Additionally, Ultralife will honor its warranty by replacing any batteries that may be determined to be defective. In the event a claim is filed against Ultralife and it is ultimately determined that Ultralife's product was defective, replacement of batteries to this Customer or end-user may have a material adverse effect on the Company's financial position and results of operations.

Item 2. Changes in Securities and Use of Proceeds

On June 4, 2003, the Company issued 125,000 shares of its common stock to an accredited investor upon conversion of a three-month $500,000 note issued on March 4, 2003 to raise funds to meet the Company's short-term working capital needs. The shares were issued in reliance on the exemption provided by Section 4(2) of the Securities Act of 1933, as amended.

Item 4. Submission of Matters to a Vote of Securities Holders

(a) On June 10, 2003, an Annual Meeting of Shareholders of the Company was held.

(b) At the Annual Meeting, the Shareholders of the Company elected to the Board of Directors all seven nominees for Director with the following votes:

| DIRECTOR | FOR | AGAINST |
|---|---|---|
| Joseph C. Abeles | 9,898,664 | 2,322,005 |
| Joseph N. Barrella | 12,183,040 | 37,625 |
| Patricia C. Barron | 12,183,040 | 37,625 |
| Daniel W. Christman | 12,182,960 | 37,705 |
| John D. Kavazanjian | 12,182,960 | 37,705 |
| Carl H. Rosner | 12,183,040 | 37,625 |
| Ranjit C. Singh | 12,181,040 | 37,625 |

(c) At the Annual Meeting, the Shareholders of the Company voted for the ratification of PricewaterhouseCoopers LLP as independent auditors with the following votes:

| FOR | AGAINST | ABSTAIN |
|---|---|---|
| 12,181,340 | 7,025 | 32,300 |

Item 6. Exhibits and Reports on Form 8-K

(a) Exhibits

10 Financing Agreement between Ultralife Batteries (UK) Ltd. and EuroFinance

99 CEO & CFO Certifications

(b) Reports on Form 8-K

On May 13, 2003, the Company filed a Form 8-K with the Securities and Exchange Commission announcing its first quarter 2003 earnings.

On May 19, 2003, the Company filed a Form 8-K with the Securities and Exchange Commission announcing the receipt of a multi-million dollar order from a major consumer products company for a private-labeled version of its popular 9-volt lithium battery. Production began in May for scheduled shipments starting in June and extending throughout 2003.

On May 21, 2003, the Company filed a Form 8-K with the Securities and Exchange Commission announcing a contract awarded for its BA-5390/U battery (previously UBI5390) valued at approximately $19 million, by the U.S. Army Communications Electronics Command (CECOM). The order represents the fourth and largest contract to date for this battery. Shipments were to began in July and will continue into the fourth quarter.

On June 12, 2003, the Company filed a Form 8-K with the Securities and Exchange Commission indicating that Company, on March 4, 2003, had issued a three-month, $500,000 note, convertible into shares of the Company's common stock at $4.00 per share, or 125,000 shares, at the option of the note holder. On June 4, 2003, the maturity date of the note, the note holder elected to convert the note into common shares and the Company had thus extinguished this debt obligation.

On June 12, 2003, the Company filed a Form 8-K with the Securities and Exchange Commission announcing orders valued at approximately $2.7 million from two of its U.S. battery distributors for its BA-5390/U lithium military battery. Shipments have begun and are expected to be completed by August.

## SIGNATURES

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

ULTRALIFE BATTERIES, INC.
(Registrant)

Date: August 8, 2003    By: /s/ John D. Kavazanjian

John D. Kavazanjian
President and Chief Executive Officer

Date: August 8, 2003    By: /s/ Robert W. Fishback

Robert W. Fishback
Vice President - Finance and Chief Financial Officer

I, John D. Kavazanjian, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Ultralife Batteries, Inc.;

2. Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this quarterly report;

3. Based on my knowledge, the financial statements, and other financial information included in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this quarterly report;

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

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

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

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

5. The registrant's other certifying officers and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent functions):

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

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

6. The registrant's other certifying officers and I have indicated in this quarterly report whether there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

Date: August 8, 2003

/s/ John D. Kavazanjian
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John D. Kavazanjian,
President and Chief Executive Officer

I, Robert W. Fishback, certify that:

1. I have reviewed this quarterly report on 10-Q of Ultralife Batteries, Inc.;

2. Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this quarterly report;

3. Based on my knowledge, the financial statements, and other financial information included in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this quarterly report;

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

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

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

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

5. The registrant's other certifying officers and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent functions):

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

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

6. The registrant's other certifying officers and I have indicated in this quarterly report whether there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

Date: August 8, 2003

/s/ Robert W. Fishback

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Robert W. Fishback
Vice President - Finance and Chief Financial Officer

Exhibit 10

Euro Sales Finance plc

This document is important. If you are in any doubt about the implications of signing this agreement you should, before you sign it, consult your solicitors or accountants concerning your obligations under the agreement.

SALES FINANCE AGREEMENT

We, Euro Sales Finance plc, whose principal office is at Smith House, P0 Box 343, Elmwood Avenue, Feitham, Middlesex, TW 13 7WH agree with you Ultralife Batteries UK Limited (registered number 02927266) of 18 Nuffield Way, Ashville Trading Estate, Abingdon, Oxfordshire, 0X14 1TG that we shall provide you with a sales finance service on the following terms and conditions and subject also to our General Conditions, "the General Conditions", which are to be treated as part of this Agreement.

1. Date: 29th April 2003

   This Agreement is made on the date it is signed by us.

2. Type of Facility

   (a) This Agreement for the sale and purchase of your book debts does not involve us (in normal circumstances) having any direct contact with your Customers and as such clauses 1(f) , 1(g), and 4.6 (b) of the General Conditions will not apply.

   (b) You will notify us of any credit notes or accounting reductions proposed to be issued or made to a Customer and will not (except with our prior permission in writing) issue or make any credit notes or reductions exceeding (pound)1,000 in aggregate.

   (c) Notwithstanding the provisions of clause 5(a) of the General Conditions you will act as our agent to collect payments due from your Customers in respect of book debts and you will deal with such payments in accordance with clause 5(c) of the General Conditions, and in any event forward collections to us forthwith upon receipt, and not bank them in any of your accounts and hold any monies or uncleared effects strictly to our order until paid over to us. This agency will cease upon the termination of this Agreement.

   (d) Upon the occurrence of a Termination Event as defined in clause 11 of the General Conditions we may at our discretion:

   notify your Customers of the assignment of their book debts to us; and/or

   terminate the agency immediately by written notice; and/or

   continue to provide you with facilities upon such terms as we may specify in writing.

   (e) Following termination of the agency, if we collect any book debts we shall be entitled to charge a collection fee at a rate of 5% of amounts so collected, without prejudice to our right to charge the Recoveries Fee but so that the total fee shall not exceed 10%

   (f) Within ten days following the end of each month you will send us, in a form we specify, an aged analysis of book debts and a copy of your sales ledger control account, together with such other documents as we may require.

3. Financial and Other Particulars

   (a) "Commencement" is

   (b) "Administration Fee" is 0.55 per cent of the Gross Invoice Value of a book debt;

   (c) "Discount" is 2.25 per cent above Royal Bank of Scotland Base Rate;

   (d) "Payment Percentage" is 70 per cent of the Gross Invoice Value of a book debt;

   (e) "Minimum Fee" is (pound)20,000;

   (f) "Arrangement Fee "is (pound)4,500.

4. Entire Agreement

   The terms set out in this Agreement represent the whole of the terms agreed between us to the exclusion of any other statements by us whether express or implied.

Signed as a deed

By Ultralife Batteries UK Limited

Director /s/ David Richards

Director/Secretary /s/ Richard Walsh

Date 30th January 2003

By Euro Sales Finance plc

Director /s/ Stuart Arenasen

Director/Secretary

Authorised signatory /s/ Natalie Williams

Date 30/4/03

SALES FINANCE SERVICE

GENERAL CONDITIONS

The clause headings used in this Agreement are for guidance only and are not intended to affect its interpretation. These General Conditions must be read in conjunction with any Agreement of which they are expressed to form part. A list of general definitions can be found in Clause 18.

1. Sale and Purchase of Debts

(a) You agree to sell or assign to us all book debts owing to you at Commencement and all your book debts arising during the life of this Agreement. We shall own your book debts from Commencement or as soon as they come into existence, even if not yet entered in your books or records as due to you. Should any book debts not come into our ownership (whatever the reason may be) you must account to us for the Debt when received and you will hold the proceeds of such debts on trust for us;

(b) You will sell or assign to us the benefit of any insurance policies relating to book debts or any goods sold or services supplied which give rise to any book debts;

(c) On signing this Agreement and as soon as a book debt arises you will notify us in the form we specify together with such information and original or copy documents proving the existence of the book debts, the delivery of goods or the performance of your services in respect of the book debts as we may request.

(d) While this Agreement continues you will not in any way sell or assign your interest in any book debts to anyone else.

(e) Should we request, you will sign, pay stamp duty on and deliver to us a document in a form that we approve legally assigning to us any book debt or debts together with the benefit of all guarantees given to you by your Customer and other related securities and, if we ask, you will immediately give written notice in a form that we approve to any Customer whose debt has been assigned in this way.

(f) You will print, stamp or otherwise mark each invoice with a notice of assignment or sale of book debts shown in a form which we shall specify.

(g) If your Customer becomes entitled to a credit or Customer discount in respect of any book debt you will notify us straight away and send to us a credit note in

respect of the credited or discounted book debt with any other documents and information which we may request. We shall be free to send the credit note to the Customer concerned or to refuse to send the credit note, which will not affect any of our other rights. In addition you will repay to us the amount of each credit note so that we are not out of pocket.

2. Disapproval and Re-Approval

Because we pay you before your Customer pays us we may at any time deduct from amounts, which we would otherwise be required to send you, a sum equivalent to any book debt previously purchased by us which looks to us as though it may be difficult for us to collect either through age, because it is disputed, or because a particular customer has exceeded either your credit limits or those which we have notified to you.

If we disapprove book debts in this way we shall be allowed to sell them back to you or re-approve them for the purposes of calculating amounts which you are entitled to draw.

3. Payments to you

At any stage during the provision of the service you will have a rolling account with us which will be calculated as follows: -

1). add the Gross Invoice Value of book debts notified to us; then

2). deduct the value of any Disapproved Debts and add the value of any reapproved debts; then

3). multiply that amount by the Payment Percentage in your agreement; then

4). deduct from that amount the value of any Advances made by us to you; then

5). deduct from that sum any Discount, Administration Fees, Disbursements or other fees due to us; then

6). add the value of any book debts received from your customers less the Payment Percentage applied to that book debt and the sum so calculated, if shown as being due to you, is your "Entitlement." Upon the occurrence of a Termination Event any further advances to you will cease automatically and from any balance due to you, we shall be entitled to deduct all commissions and expenses as provided in this Agreement.

4. Charges

4.1. Charges will arise either as Discount, Fees or Disbursements as follows:

(a) Discount will be charged on a basis similar to that upon which simple interest is calculated at a margin ( %) over The Royal Bank of Scotland base rate from time to time.

b) Discount will be charged on the daily balance outstanding and due from you to us accrued on a daily basis and invoiced monthly in arrears.

(c) Any receipt from your Customer will be credited to your account with us four working days after the day of banking, but not including the day of banking.

(d) Payments made to you will be debited from your account with us on the day on which they are made whether the payment is made to you by cheque or bank transfer.

4.2 Fees

(a) We shall charge Administration Fees as a percentage of the Gross Invoice Value.

(b) Occasionally Administration Fees may be charged on a fixed monthly basis, monthly in advance.

(c) We may agree with you to charge you an arrangement fee to cover our initial costs in setting up your facility.

4.3. Minimum Fees

We may charge a minimum turnover fee in the event that your turnover of Gross Invoice Value in the 12 month period following the commencement of the provision of the Sales Finance Service or any subsequent 12 month period falls below a pre-determined minimum. This may be charged monthly in advance on a pro rata basis at our discretion.

4.4. Bank Fee

We shall charge (pound)25 each time funds are transferred by banker's transfer to your account with your clearing bankers.

4.5. Over-payment Fees

We may agree with you to charge over payment fees when you require funds in excess of your agreed Entitlement from time to time.

4.6. Recoveries Fee

(a). If you cease to trade or if you suffer the appointment of an administrator, administrative receiver, a liquidator, or if you propose a voluntary arrangement or winding up of your company, then we shall be entitled to charge a recoveries management fee which is equivalent to 10% of the Gross Invoice Value of monies collected, to reflect the increased cost of collection in the event of insolvency or cessation of trading.

(b) We shall charge you a late payment fee of 0.5% on all book debts due from your Customers which are more than 90 days old, invoiced monthly in arrears.

4.7. Disbursements

(a). We shall deduct from your entitlement all disbursements which are clearly identifiable as being attributable to you and which are not covered by our normal service. These may include matters such as credit reference fees, legal fees for debt recovery and other such matters, but they will not include travelling costs, stationery costs and our bank charges or indeed our overheads.

(b). Disbursements however will include any costs incurred by us in appointing investigating accountants and lawyers.

5. Collection from Customers

(a). From the commencement of the Sales Finance Service we shall have the sole and exclusive right to collect and enforce payment of every book debt other than debts sold back to you and you have no right to collect book debts unless we authorise you to do so in advance in writing.

(b). You will assist our collection efforts if we so request by providing all information required and you agree that for collection purposes we may institute and conduct legal proceedings in your name under our full control. We shall of course liaise with you but shall not be under any duty to do

(c). You will immediately pass to us or to any Bank we direct any payment a Customer makes to you directly in respect of a book debt and you agree not to mark or endorse any negotiable instrument relating to such payment otherwise than in our favour. You will hold any payment you receive for a book debt on trust for us until we receive it. You must not bank any such payment for your own account.

(d). If a Customer makes a general payment either to us or to you without specifying which debts are covered by it then we shall apply it firstly against any book debts outstanding and secondly against the discharge of your liability to us, if any, whether arising under this Agreement or otherwise, and any balance shall be paid as you wish.

(e). If there is shown in our books a credit balance with any Customer which remains outstanding we shall be entitled at our discretion to make repayments of such credit balance to the Customer out of monies available to you.

(f). If any book debt received from any Customer is received by us in a currency other than sterling and the amount produced by converting the other currency to sterling is less than the amount of any sum advanced by us in relation to the book debt in question then we shall be entitled to recoup any such short fall from any Entitlement and you will in any event as an independent obligation indemnify us for the deficiency and any loss sustained as a result. Unless agreed by us in writing in advance any payments due hereunder shall be made in sterling. Any such conversion shall be made at the prevailing rate of exchange on the date of clearance of any effects banked by us in such market as is determined by us as being most appropriate for such conversion, and you will in addition pay to us, or we shall be entitled to deduct from your Entitlement any costs of such conversion.

6. Disputed Goods

If any goods relating to any book debt are returned by a Customer or delivery is refused or the goods are rejected or repossessed by you, you agree to transfer to us all your right title and interest in such goods and, you will put those goods on one side, mark them

clearly and prominently with our name as owner and hold them strictly to our order until they are resold at our direction or until we are fully reimbursed in relation to any book debt in respect of such goods.

7. Accounts and Set-Off

(a). We shall keep a permanent record to show all sums payable or paid to you, all payments received in relation to book debts and all fees, expenses and other sums payable or paid by you under this Agreement or otherwise. No later than 10 working days from the last day of each month we will send to you a copy of such account which shall be taken as undisputed evidence of the matters stated in it at the date of its preparation unless within 14 days from despatch you notify us in writing of any discrepancy. This account shall be your invoice for VAT purposes.

(b). We may at any time draw up an account to record all amounts due to you from us and to us from you.

(c). We may at any time set off any moines due to us from you whether pursuant to this Agreement or otherwise against any sums due from us to you. We shall only ever be obliged to pay you sums which are net of any discount costs fees and disbursements due to us.

8. Accounting and Access Information

You agree that you will:

(a). keep fully detailed, up-to-date and proper accounting records and allow us to enter your premises whenever we wish to inspect them and such other papers as we may wish relating to your business debts generally and allow us to take possession of such material to enable us to make copies provided that we return such material to you within a reasonable time;

(b). cause a proper audit to be completed of the books of account for yourself and your subsidiaries, if any, for each financial year and send an audited report and accounts to us as soon as they are available and in any event within three months from the end of each financial year;

(c). keep us informed at all times of the credit worthiness of your Customers and the validity of each book debt and in particular of any counter-claims, right of set off or other contra items raised by your Customers in relation to any book debt and assist us in every way to safeguard our interests;

(d). as and when produced, send us management accounts for your business and at our request for any Related Company in a format and at intervals acceptable to us;

(e). if we require, send to us within 10 days from the end of each month an aged list of your creditors or a copy of your bought ledger;

(f). report to us immediately about reclaimed, repossessed or returned merchandise, Customers' claims and disputes, and any other matters affecting any book debts;

(g). provide us with specimen signatures of persons authorised to sign any documents relating to this Agreement together with a Board resolution authorising for this purpose such persons and inform us immediately of any change in the signatories;

(h). give us a signed letter in our prescribed form for all existing bank accounts (and whenever you open a new bank account) requesting the bank to pay over to us monies received directly from your Customers;

(i). notify us in writing

as soon as you become aware of any event which affects or may affect your warranties or our rights of immediate termination;

of any existing mortgages charges liens or other security over your assets;

immediately when there are any changes in the nature of your business, your directors or company secretary or a material change in your ownership (a holding by a person, firm or company of 10 per cent or more of your equity is for this purpose deemed to be material);

of any company which becomes or ceases to be a Related Company;

of any Customer which is your associate or an associate of any of your directors or might otherwise fairly be regarded as connected to you or any of your directors;

of the terms upon which any goods are supplied to you and obtain such waivers or variation to such terms as we may require.

If any customer also becomes a supplier to you or to any Related Company.

9. Warranties

You warrant in respect of each book debt that:-

(a). you will not waive or modify your normal trading terms with any Customer without obtaining our prior written consent and in particular you will not extend the time for payment;

(b). we shall obtain a valid binding and enforceable title to the full amount owing to you on each book debt sold or assigned us and to all assigned rights and remedies included in the sale of the book debt to us and that no supplier to you will retain title to any goods sold by you which are the subject matter of a book debt;

(c). you have already performed all the obligations required for enforcement of the book debt including delivery of goods or performance of services;

(d). your Customer will pay the full amount of each book debt no later than 90 days after the date of invoice;

(e). your Customer has an established place of business and your debtors are not connected or associated with you and have no right which would reduce or extinguish the Gross Invoice Value of the book debt.

10. Power of Attorney

You irrevocably appoint us as your attorney both during and after termination of this Agreement to act in your name and on your behalf to execute all documents and do all things necessary to give effect to this Agreement or our rights including making any arrangement or compromise, taking or defending any proceedings endorsing any negotiable instrument on your behalf and executing legal assignments of all or any book debt. This means that we can act on your behalf without reference to you in connection with the collection of book debts.

11. Duration of Agreement

This Agreement will remain in operation from Commencement-until either you give us seven days notice or we give you three months notice, to terminate this Agreement and subject to our rights of immediate termination set out below.

We may by giving you written notice terminate this Agreement forthwith if:

(a). you commit a breach of any term of this Agreement; or

(b). the nature or volume of your business is in our view substantially changed; or

(c). there is any change in the person or persons who Control you; or

(d). any of our payments to you are not used in the ordinary course of your business; or

(e). any monies owing from you to us are not paid within 7 days after they become due; or

(f). any distress or execution or attachment is levied upon any of your goods or premises or any garnishee order is made on any person indebted to you; or

(g). a receiver or administrative receiver is appointed over any of your assets; or

(h). you become insolvent; or

(i). you convene a meeting for the purpose of passing a resolution for creditors voluntary winding up, or are the subject of a compulsory winding up order or a petition for an administration order is presented and you cease to carry on business or call a meeting of creditors to make an arrangement or composition with creditors or permit a judgement to remain unsatisfied for seven days; or

(j). we in our absolute discretion consider that your financial position has deteriorated to the point at which we believe that repayments of any amounts due or which may become due from you to us may be put at risk. Any reference in this clause to you shall be taken to include any of your subsidiaries.

12. Consequence of Termination

(a). Termination of this Agreement will not affect the rights or obligations of either you or us in relation to any book debt and this Agreement will continue to bind us both as long as it is necessary to satisfy these rights and obligations.

(b). In the event of termination or upon the occurrence of a termination event then without prejudice to our accrued rights and remedies under this Agreement you agree to pay us forthwith upon written demand a sum equal to the amount of all payments we have made to you under this Agreement plus all fees and charges which have accrued during the Agreement less the amounts which we have received from your Customers and which have been allocated to your account with us.

(c). In the event of termination or upon the occurrence of a termination event we may retain any amount received by us in respect of any book debt pending the drawing up of a final account and the payment of any amount consequently due to us.

(d). Following the drawing up of a final account and any consequent payment to us we shall re-assign to you without payment any book debt still outstanding.

13. Security

You will grant us such fixed or floating charges as we may from time to time require as security for the payment of all sums due or becoming due to us under this Agreement and you will not give any new charge or other security to any third party without first obtaining our written consent.

14. Indemnity

You agree to indemnify us against any claim by a Customer and any loss incurred by us as a result of our entering into this Agreement. No waiver forbearance or indulgence granted by us to you or to any Customer will in any way discharge you from your liabilities to us to establish a precedent.

15. Transfer of Rights

We shall be entitled to assign or charge this Agreement or any of our rights and obligations hereunder. You may not assign or otherwise deal with this Agreement or your rights and obligations hereunder without our prior written consent.

16. Variation

This Agreement may only be varied by a document signed by us and by you.

17. Applicable Law and Notices

This Agreement is to be interpreted in accordance with and governed by English Law. Any notices to be given by either of us to the other may be either delivered by hand to the other party or its authorised agent or sent by pre-paid first class letter, registered post, recorded delivery fax transmission or telex to such party as its principal place of business or at its registered office.

18. Interpretation

'Administration Fee' means the sum prescribed in clause 4.2 and your Sales Finance Agreement;

'Approved Debt' means any book debt in respect of which the Payment Percentage has been advanced or is payable and which has not been disapproved by us or which was previously Disapproved and has since been Reapproved. 'Approve' in relation to any Debt will be construed accordingly;

'Associate' means any relative, partner, director, shareholder or employee of you or of any Related Company;

'Control' means the power to secure that the affairs of a company or a group of people are conducted in accordance with the wishes of those holding such power;

'Customer' means any person to whom you supply goods or for whom you perform services;

'book debt' means an amount which is owed to you for goods supplied or services performed calculated at Gross Invoice Value and includes the benefit of the sale or supply contract relating to such goods or services and all rights and remedies arising in connection with such contract including retention of title to goods, right of lien, stoppage in transit, or recover of possession;

'Disapproved Debt' means any book debt which, in our absolute discretion, we exclude for the purpose of calculating any payment due to you and 'disapprove' in relation to any book debt shall be construed accordingly;

'Gross Invoice Value' of a book debt is the total amount thereof including VAT and before taking into consideration any allowances in respect of discounts for prompt payment or any other allowable deduction;

'Payment Percentage' means the amount (subject to adjustment) payable on notification of an Approved Debt;

'Related Company' means a company which either you Control or which Controls you or which is Controlled by the same person, firm or company which Controls you;

'Commencement' is the date when this Agreement commences;

'Termination Event' means any of the events described in clause 11.

Signed and acknowledged by Ultralife Batteries UK Limited

Director /s/ David Richards

Director/Secretary /s/ Richard Walsh

Date 30th January 2003

Dated 30th April 2003

# DEBENTURE

- made between -

Ultralife Batteries UK Limited (1)

Euro Sales Finance plc (2)

THIS DEBENTURE is made the

BETWEEN:

(1) Ultralife Batteries UK Limited a company incorporated in England (registered number 02927266) whose registered office is at 18 Nuffield Way, Ashville Trading Estate Abingdon, Oxfordshire OX 14 1TG ("the Client")

(2) Euro Sales Finance plc a company incorporated in England (registered number 3038707) whose registered office is at Smith House, P0 Box 343, Elmwood Avenue, Feitham, Middlesex, TW13 7WH ("ESF").

NOW THIS DEED WITNESSES as follows:

1. Definitions and Interpretation

1.1 In this Deed the following words and expressions shall, unless the context otherwise requires, have the following meanings:

'Charged Assets' means the assets charged under Clause 3;

'Deed' means this document, including its recitals and the Schedule;

'Full Title Guarantee' means full title guarantee as that expression is defined in the Law of Property (Miscellaneous Provisions) Act 1994;

'Receiver' means an administrative receiver, receiver and manager or other receiver appointed in respect of the Charged Assets;

'LPA' means the Law of Property Act 1925;

'Property' means the property, short particulars of which are set out in the Schedule;

'Secured Obligations' means all sums and liabilities covenanted to be paid and discharged by the Client;

'Security Interest' means any

mortgage, charge, pledge, lien encumbrance, security interest or other security arrangement of any kind.

1.2 Unless the context requires otherwise, or unless otherwise defined in this Deed, words and expressions defined in ESF's General Conditions shall have the same meanings when used in this Deed.

1.3 Any reference to a statutory provision is a reference to that provision as for the time being extended, modified or re-enacted.

1.4 Headings in this Deed are for convenience only and shall not affect its interpretation. Words importing the plural shall include the singular and vice versa.

1.5 In this Deed the expressions "Client" and "ESF" shall include their respective successors, assigns or transferees.

2. Covenant to Pay

The Client hereby that it will on demand discharge all obligations and liabilities whether actual or contingent now or at any time hereafter due owing or incurred to ESF by the Client anywhere in any manner whatsoever (whether alone or jointly and in whatever style, name or form and whether as principal or surety) together with interest at the rate of 3 per cent per annum above the base rate for the time being of Bank of Scotland on any late payment (as well after as before any demand or judgement) calculated and compounded in accordance with ESF's usual practice and all legal and other costs charges and expenses incurred by ESF in relation to the Client on a full and unqualified indemnity basis.

3. Charging Provisions

3.1 The Client by way of continuing security for the payment and discharge of the Secured Obligations hereby charges to ESF with full title guarantee: -

3.1.1 by way of first fixed charge:-

(a). all book and other debts both present and future at any time due or owing to the Client and the full benefit of all rights and remedies relating thereto; and

(b). all benefits in respect of all contracts and policies of insurance whatever nature in relation to the assets charged by clause 3.1.1(a) above which are from time to time taken out by the Client or in which the Client has an interest.

3.1.2 by way of first floating charge the undertaking and all property, assets and rights of the Client whatsoever and whatsoever both present and future which is or may be from time to time while this Deed is in force comprised in the property and undertaking of the Client including, without limitation, the property and assets and rights of the Client referred to in Clauses 3.1.1 above inclusive (if and in so far as the charges therein contained shall for any reason be ineffective as fixed charges).

3.2 ESF may at any time by notice in writing to the Client convert the floating charge into a specific charge as regards any assets specified in the notice which ESF may consider to be in danger of being seized or sold under any form of distress execution or other process levied or threatened and may appoint a Receiver thereof.

4. Continuing Security

This security shall be a continuing security notwithstanding any settlement of account or other matter whatsoever and is in addition to and shall not merge with or otherwise prejudice any contractual or other right or remedy or any other security now or hereafter held by or available to ESF and shall not be in any way prejudiced or affected thereby or by ESF now or hereafter dealing with, exchanging, releasing, varying or abstaining from perfecting or enforcing any of same or any rights which they may now or hereafter have or giving time for payment or indulgence or compounding with any other person liable.

5. Restrictions on Dealing

The Client hereby covenants that it will not save with the prior written consent of ESF:

5.1 sell, assign, discount, factor, pledge, charge or otherwise dispose of the property and assets referred to in Clause 3.1.1(a) or 3.1.1(b) or any part thereof or deal with the same;

5.2 create or permit to subsist any Security Interest upon or affecting any of its undertaking, property or assets (other than this Debenture); and

5.3 part with possession, transfer, sell or otherwise dispose of or attempt or agree to transfer, sell or otherwise dispose of the whole or any part of its undertaking, property, assets or rights except in the usual course of trading and for the purpose of carrying on its business.

6. Covenants

6.1 The Client hereby covenants with ESF that during the continuance of this security the Client will at all times:

6.1.1 conduct and carry on its business in a proper and efficient manner and keep or cause to be kept proper books of account relating to such business;

6.1.2 furnish to ESF copies of its trading and profit and loss account and audited balance sheet in respect of each financial year forthwith upon the same becoming available and such other financial statements and information of the Client as ESF may require; and

6.1.3 punctually pay and indemnify ESF and any Receiver appointed by it against all rents, rates, taxes, duties, charges, assessments, impositions and outgoings whatsoever now or at any time during the continuance of this security payable in respect of the Charged Assets or any part thereof by the owner or occupier thereof. If any such sums shall be paid by ESF or by any such Receiver the same shall be repaid by the Client on demand.

6.2 The Client hereby further covenants with ESF that during the continuance of this security the Client will:

6.2.1 get in and realise in the ordinary course of business all book and other debts hereby charged and pay the same into any account nominated by ESF from time to time in accordance with the General Conditions or any other agreement between the Client and ESF; and

6.2.2 deposit with ESF and permit ESF during the continuance of this security to hold and retain the following all such documents relating to the Charged Assets as ESF may from time to time require.

7. Further Assurance

The Client shall whenever requested by ESF execute and sign all such deeds and documents and do all such things as ESF may require at the Client's cost over any property or assets specified by ESF for the purpose of perfecting or more effectively providing security to ESF for the payment and discharge of the Secured Obligations.

8. When Security Becomes Enforceable

8.1 The security hereby conferred will become immediately enforceable and the power of sale and other powers conferred by Section 101 of the LPA as amended or varied by this Deed shall be immediately exercisable:

8.1.1 at any time after the Client's late payment or failure to discharge any of the Secured Obligations or any part thereof including failure to meet any demand made in accordance with this Deed; or

8.1.2 if the Client shall have been in default of any of its obligations hereunder; or under any other agreement between the Client and ESF;

8.1.3 upon crystallisation of the floating charge created by Clause 3.1.2; or

8.1.4 if the Client shall request that ESF shall appoint a Receiver; or

8.2 After this Deed shall have become enforceable ESF may in its absolute discretion enforce all or any part of the security constituted hereby in such manner as it sees fit.

9. Enforcement of Security

9.1 The statutory power of sale and of appointing a Receiver conferred on mortgagees by Section 101 of the LPA, as varied and extended by this Deed, shall be deemed to arise on the date of this Deed and in favour of any purchaser or other person shall be deemed to be exercisable on and from the date of this Deed. Section 93 (restricting the right of consolidation) and Section 103 (restricting the power of sale) of the LPA shall not apply to this Deed.

9.2 The statutory powers of leasing conferred on ESF shall be extended so as to authorise ESF to lease, make agreements for leases, accept surrenders of leases and grant options as ESF shall think fit and without the need to comply with any of the provisions of Sections 99 and 100 of the LPA.

10. Appointment and Powers of a Receiver

10.1 At any time after the security constituted by this Deed has become enforceable ESF may by written notice appoint any person to be a Receiver of the Charged Assets or any part thereof (with power to authorise any joint Receiver to exercise any power independently of any other joint Receiver) and may from time to time fix his or their remuneration and may remove any Receiver so appointed and appoint another or others in his place.

10.2 Any Receiver so appointed shall be the agent of the Client and the Client shall be solely responsible for his acts or defaults and for his remuneration.

10.3 Any Receiver so appointed shall have all powers conferred by the LPA (without the restrictions contained in Section 93 and 103 of that Act) and the Insolvency Act 1986 on mortgagors, mortgagees in possession (but without liability as such), receivers, administrative receivers and administrators appointed under those Acts. In addition the Receiver shall have power on behalf and at the cost of the Client (notwithstanding any liquidation of the Client) to do or omit to do anything which the Client could do or omit

to do in relation to the Charged Assets or any part thereof and in particular (but without prejudice to the generality of the foregoing) any such Receiver may:

10.3.1 take possession of, collect and get in all or any part of the property in respect of which he is appointed and for that purpose to take any proceedings;

10.3.2 carry on or concur in carrying on the business of the Client and to raise money from ESF or others on the security of any of the Charged Assets;

10.3.3 sell or concur in selling, let or concur in letting and terminate or accept surrenders of leases and tenancies of any of the Charged Assets and to carry any such transactions into effect;

10.3.4 sell, assign, let or otherwise dispose of or concur in selling, assigning, letting or otherwise disposing of all or any of the debts and any other property in respect of which he is appointed;

10.3.5 make any arrangement or compromise between the Client and any other person which he may think expedient;

10.3.6 make and effect all repairs, improvements and insurances;

10.3.7 purchase materials, tools, equipment, goods or supplies;

10.3.8 call up any uncalled capital of the Client with all the powers conferred by the Articles of Association of the Client in relation to calls;

10.3.9 employ, engage and appoint managers and other employees and professional advisers; and

10.3.10 do all such other acts and things as may be considered to be incidental or conducive to any other matters or powers aforesaid or to the realisation of the security constituted by this Deed and which he lawfully may or can do.

10.4 All money received by ESF or by such Receiver in the exercise of any powers conferred by this Deed shall be applied after the discharge of the remuneration and expenses of the Receiver and all liabilities having priority thereto in or towards satisfaction of such of the Secured Obligations and in such order as ESF in its absolute discretion may from time to time conclusively determine (save that the Receiver may retain the same for such period as he and ESF consider expedient). No purchaser or other person shall be bound or concerned to see or enquire whether the right of ESF or any Receiver or Manager appointed by them to exercise any of the powers hereby conferred has arisen or not or be concerned with notice to the contrary.

10.5 any such receiver shall be entitled to remuneration appropriate to the work and responsibilities involved upon the basis of charging from time to time adopted by the receiver in accordance with the current practice of his firm without being limited to the maximum rate specified in section 109(6) of the law of property act 1925.

10.6 the client hereby covenants with ESF on demand to pay all costs charges and expenses incurred by ESF or by any such receiver or which it or he shall properly incur in or about the enforcement preservation or attempted preservation of this security or of the

charged assets or any of them on a full indemnity basis including any costs incurred by the receiver before his appointment in his capacity of investigating accountant.

10.7 neither ESF nor any such receiver shall be liable to account as mortgagee in possession in respect of all or any of the charged assets nor be liable for any loss upon realisation or for any neglect or default of any nature whatsoever in connection therewith for which a mortgagee in possession may be liable as such.

10.8 the client hereby agrees to indemnify and hold harmless both ESF and any such receiver from and against all actions, claims, expenses, demands and liabilities whether in contract, tort or otherwise now or hereafter incurred by it or him or by any manager agent officer or employee for whose liability act or omission it or he may be answerable for anything done or omitted in the exercise or purported exercise of the powers herein contained.

11. Powers of ESF

ESF may exercise without further notice and whether or not it shall have appointed a Receiver all the powers conferred upon mortgagees by the LPA as hereby varied or extended and all the powers and discretions hereby conferred expressly or by implication on a Receiver appointed hereunder.

12. Power of Attorney

By way of security, the Client irrevocably appoints ESF and any Receiver jointly and severally as its Attorney, with full power of delegation for it and in its name and on its behalf and as its act and deed or otherwise, to seal, deliver and otherwise perfect any deed, assurance, legal assignment, agreement, instrument or act which may be required or may be deemed proper for any of the purposes set out in this Deed.

The Client shall ratify and confirm all transactions entered into by ESF, any Receiver, or any delegate of ESF in the exercise or purported exercise of ESF's or Receiver's respective powers and all things done by ESF, such Receiver or delegate by virtue of any power of attorney given herein.

13. Set-off

ESF may at any time and without notice to the Client combine or consolidate all or any of the Client's then existing accounts with and liabilities to ESF and set-off or transfer any sum or sums standing to the credit of anyone or more of such accounts in or towards satisfaction of any of the Secured Obligations. ESF shall notify the Client that such a transfer has been made.

ESF may at any time and without notice to the Client set-off any obligation owed by ESF to the Client against the whole or part of the Secured Obligations.

14. New Accounts

If ESF receives notice of any subsequent Security Interest affecting the Charged Assets or any part thereof or interest therein ESF may open a new account for the Client. If ESF does not open a new account then unless ESF gives express written notice to the contrary to the Client it shall nevertheless be treated as if it had done so at the time

when it received such notice and as from that time all payments made by or on behalf of the Client to ESF shall be credited or be treated as having been credited to the new account and shall not operate to reduce the amount due from the Client to ESF at the time when it received notice.

15. Currency Clauses

15.1 All moneys received or held by ESF or by a Receiver under this Deed may from time to time after demand has been made by ESF be converted into such other currency as ESF considers necessary or desirable to cover the obligations and liabilities actual or contingent of the Client in that other currency at the then prevailing spot rate of exchange obtainable by ESF (as conclusively determined by ESF) for purchasing that other currency with the existing currency.

15.2 If and to the extent that the Client fails to pay the amount due on demand ESF may in its absolute discretion without notice to the Client purchase at any time thereafter so much of any currency as ESF considers necessary or desirable to cover the obligations and liabilities of the Client in such currency hereby secured at the then prevailing spot rate of exchange obtainable by ESF (as conclusively determined by ESF) for purchasing such currency with sterling and the Client hereby agrees to indemnify ESF against the full sterling cost incurred by ESF for such purchase.

15.3 No payment to ESF (whether under any judgement or court order or otherwise) shall discharge the obligation or liability of the Client in respect of which it was made unless and until ESF shall have received payment in full in the currency in which such obligation or liability was incurred and to the extent that the amount of any such payment shall on actual conversion into such currency falls short of such obligation or liability actual or contingent expressed in that currency ESF shall have a further separate cause of action against the Client and shall be entitled to enforce the charges hereby created to recover the amount of the shortfall.

16. Miscellaneous

16.1 All the provisions of this Deed are severable and distinct from one another and if at any time one or more of such provisions is or becomes invalid illegal or unenforceable the validity legality and enforceability of the remaining provisions hereof shall not in any way be affected or impaired thereby.

16.2 No payment to ESF (whether under any judgement or order of any Court or otherwise) shall discharge the obligation or liability of the Client in respect of which it was made unless and until ESF shall have received payment in full and to the extent that the amount of any such payment shall fall short of such obligation or liability ESF shall have a further separate cause of action against the Client and shall be entitled to enforce the charges hereby created to recover such sum as shall pay the amount of the shortfall.

16.3 No failure or delay by ESF in exercising any right or remedy shall operate as a waiver thereof nor shall any single or partial exercise or waiver of any right or remedy preclude its further exercise or the exercise of any other right or remedy as though no waiver had been made and no relaxation or indulgence granted.

16.4 It is hereby certified that neither the execution of this Deed nor the creation of the charges herein contained contravenes any of the provisions of the Memorandum and Articles of Association or other constitutional documents of the Client.

16.5 Any change in the constitution of ESF or its absorption in or amalgamation with any other person or the acquisition of all or part of its undertaking by any other person shall not in any way prejudice or affect its rights hereunder.

17. Notices

Any notice to be given under this Deed shall either be delivered personally or sent by first class recorded delivery post, tested telex or facsimile transmission. The address of the service of each party shall be the address stated in this Deed or such other address as it shall have from time to time notified to the other party. A notice shall be deemed to have been served as follows:

17.1 if personally delivered, at the date of delivery;

17.2 if posted, at the expiration of 48 hours after the envelope containing the same was delivered into the custody of the postal authority; and

17.3 if sent by telex of facsimile transmission, at the time of transmission.

18. Governing Law

This Deed shall be governed by and interpreted in accordance with English law in every particular matter and any proceedings arising out of or in connection with it may be brought in any court of competent jurisdiction in England. IN WITNESS whereof each of the parties hereto has executed and delivered this Deed the day and year first before written.

THE COMMON SEAL of \ SIGNED as a DEED by
Ultralife Batteries UK Limited
was hereunto affixed in the presence of

Director /s/ David Richards

Secretary /s/ Richard Walsh

30th January 2003

THE COMMON SEAL of \ SIGNED as a DEED by
Euro Sales Finance plc
was hereunto affixed in the presence of:

Director /s/ Stuart Arenasen

Director/Secretary

Authorised signatory /s/ Natalie Williams

30th April 2003

Formal Offer

| | |
|---|---|
| Facility: | Confidential Shadow Ledger Recourse |
| Provided by | Euro Sales Finance plc - A member of The Royal Bank Of Scotland Group |
| On Behalf of: | Ultralife Batteries UK Limited |
| FACILITY PARAMETERS | This offer has been prepared with all figures quoted in GBP |
| Minimum Agreement Period: | 12 Months from the date of this agreement |
| Minimum Notice Period: | 6 Months |
| Funding Period: | 90 days end of month from invoice date |
| Sales Territories: | United Kingdom<br>Europe<br>Rest Of World |
| Sales Ledger Currency: | GBP |
| Funding Cap: | Yes Amount:(pound)450,000 |
| Initial Prepayment: | UK Sales - 70% of approved eligible debts |
| Non-Notifiable Debts: | Cash, pro-forma & credit card sales. Exports to non-OECD countries. Sales to Associated Companies (Ultralife Batteries Inc.) Sales to customers who are also suppliers. Sales to customers in the USA who receive prod, directly from Ultralife Batteries Inc. |
| ANTICIPATED CLIENT PROFILE | |
| Projected Annual Turnover (inc. VAT): | (pound)5,500,000 (excluding non-notifiable debts) |
| Customer Credit Terms | Standard: 30 days from date of invoice |
| Exceptional: | 60 days from date of invoice |

| CHARGE FOR SERVICES | 60 days from date of invoice |
| --- | --- |
| Proposed Commission Charge: | 0.55% per annum<br>Subject to VAT at the standard rate and expressed as a percentage of gross annual sales turnover. |
| Minimum Commission Charge: | (pound)20,000 per annum<br>Subject to VAT at the standard rate. |

CHARGE FOR FINANCE

| Discounting Charge: | 2.25% per annum<br>Expressed over The Royal Bank of Scotland Plc base rate currently 4.00% |
| --- | --- |
| Arrangement Fee: | (pound)4,500 (plus VAT)<br>Payable upon commencement of this Agreement |

PRECOMMENCEMENT CONDITIONS

Letter of continued support from Ultralife Batteries Inc.

Waiver from Congress Financial Corporation in respect of the trade receivables.

Deed of postponement from Ultralife Batteries Inc. in respect of interest bearing loan and trade creditor balance.

ENDURING OPERATIONAL/SPECIAL CONDITIONS

ESF will require copies of your management accounts on a quarterly basis to include a profit & loss account and balance sheet. These are to be provided no later than 6 weeks from the quarter end.

ESF will require you to obtain proof of delivery for all invoices raised & funded by us. These documents are to be retained by you & held to our order, ESF, at its absolute discretion, may request copies of these documents from time to time.

Debtor concentration limits will be 15%. MOD Concentration limit will be 30% of the approved eligible debt. Separate application to this can be made on an on-going basis,

Our facility is reliant on your credit control & collection systems being correctly implemented. We would not, therefore, expect to see a month when your sales ledger debt turn exceeded 80 days (excluding intercompany sales receivables). Should this happen, we shall reduce your prepayment facility according to the following formula:

Actual days outstanding = 82 days
2 divided by 80 days x 100% = 3%
Your pre-payment facility will reduce to 67% in the following month.

The terms & conditions set out above may be varied according to the following criteria:

1. The operation of the Agreement.
2. The standard of the proof of debt.
3. The financial standing of the Company

There will be a Maximum Funds In Use (MAFIU) of(pound)450,000 for the Company.

Please indicate your acceptance of these terms and conditions by signing and dating below and by initialling and dating all other pages of the Formal Offer. Please retain the second copy for your information. We accept the terms of your quotation and the conditions attached hereto

Signed: /s/ Richard Walsh Dated: 30th January 2003

For and on behalf of: Ultralife Batteries UK Limited

Exhibit 99

Certification pursuant to Section 1350 of Chapter 63
of Title 18 of the United States Code
as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

I, John D. Kavazanjian, President and Chief Executive Officer of Ultralife Batteries, Inc., hereby certify that (i) the Quarterly Report on Form 10-Q for the period ended June 28, 2003 attached hereto fully complies with the requirements of Sections 13(a) or 15(d) of the Securities Exchange Act of 1934, and (ii) the information contained in the attached Form 10-Q fairly presents, in all material respects, the financial conditions and results of operations of Ultralife Batteries, Inc. for the period presented therein.

A signed original of this written statement required by Section 906 has been provided to Ultralife Batteries, Inc. and will be retained by the Company and furnished to the Securities and Exchange Commission on request.

Dated: August 8, 2003 /s/ John D. Kavazanjian

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John D. Kavazanjian
President and Chief Executive Officer

Certification pursuant to Section 1350 of Chapter 63
of Title 18 of the United States Code
as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

I, Robert W. Fishback, Vice President of Finance and Chief Financial Officer of Ultralife Batteries, Inc., hereby certify that (i) the Quarterly Report on Form 10-Q for the period ended June 28, 2003 attached hereto fully complies with the requirements of Sections 13(a) or 15(d) of the Securities Exchange Act of 1934, and (ii) the information contained in the attached Form 10-Q fairly presents, in all material respects, the financial conditions and results of operations of Ultralife Batteries, Inc. for the period presented therein.

A signed original of this written statement required by Section 906 has been provided to Ultralife Batteries, Inc. and will be retained by the Company and furnished to the Securities and Exchange Commission on request.

Dated: August 8, 2003 /s/ Robert W. Fishback

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Robert W. Fishback
Vice President - Finance and Chief Financial Officer