

A.P. PHARMA, INC.

NOTICE OF ANNUAL MEETING OF STOCKHOLDERS
TO BE HELD MAY 31, 2006

To the Stockholders of A.P. Pharma, Inc.:

The Annual Meeting of Stockholders of A.P. Pharma, Inc. (the "Company") will be held at the corporate offices at 123 Saginaw Drive, Redwood City, California 94063, on May 31, 2006, at 9:00 a.m. local time, for the following purposes:

1. To elect seven directors to hold office until the next Annual Meeting of stockholders and until their successors are elected.
2. To amend the Company's 1997 Employee Stock Purchase Plan to increase by 150,000 the number of shares of common stock reserved for issuance under the Plan.
3. To amend the Company's 2002 Equity Incentive Plan to increase by 400,000 the number of shares of common stock reserved for issuance under the Plan.
4. To ratify the appointment of Odenberg, Ullakko, Muranishi & Co., LLP as A.P. Pharma's independent registered public accounting firm.
5. To transact such other business as properly may come before the meeting, or any adjournments or postponements of the meeting.

Only stockholders of record at the close of business on April 5, 2006, are entitled to notice of, and to vote at, the meeting and any adjournments or postponements of the meeting. A list of such stockholders will be open to examination by any stockholders at the Annual Meeting and for a period of ten days prior to the Annual Meeting during ordinary business hours at the offices of the Company located at 123 Saginaw Drive, Redwood City, California 94063.

BY ORDER OF THE BOARD OF DIRECTORS,

Julian N. Stern, Secretary

Redwood City, California
April 26, 2006

- IMPORTANT -

WHETHER OR NOT YOU EXPECT TO ATTEND THE MEETING IN PERSON, PLEASE COMPLETE, SIGN, DATE AND RETURN THE PROXY CARD IN THE ENCLOSED POSTPAID ENVELOPE OR FOLLOW THE TELEPHONE OR INTERNET VOTING INSTRUCTIONS ON THE PROXY CARD AS SOON AS POSSIBLE. THANK YOU FOR ACTING PROMPTLY.

A.P. PHARMA, INC.
123 Saginaw Drive
Redwood City, California 94063
(650) 366-2626

PROXY STATEMENT

The enclosed proxy is solicited on behalf of the Board of Directors (the "Board") of A.P. Pharma, Inc. ("APP" or the "Company"), a Delaware corporation. The proxy is solicited for use at the Annual Meeting of Stockholders (the "Annual Meeting") to be held at 9:00 a.m. local time on May 31, 2006, at the Company's corporate offices at 123 Saginaw Drive, Redwood City, California 94063. The approximate date on which this proxy statement and the accompanying notice and proxy are first being mailed to stockholders is April 26, 2006.

VOTING

Only stockholders of record at the close of business on April 5, 2006, are entitled to notice of, and to vote at, the Annual Meeting and any adjournments or postponements thereof. At the close of business on that date, the Company had outstanding 25,301,047 shares of its Common Stock, \$.01 par value (the "Common Stock"). Holders of a majority of the outstanding shares of Common Stock of the Company, either present in person or by proxy, will constitute a quorum for the transaction of business at the Annual Meeting.

Holders of Common Stock are entitled to one vote for each share of Common

Stock held. Stockholders do not have cumulative voting rights. In the election of directors, the seven nominees receiving the highest number of affirmative votes of the shares present and voting at the Annual Meeting at which a quorum is present will be elected directors.

Abstentions are included in the determination of whether a quorum is present at the meeting and are counted in tabulations of the votes cast on proposals presented to stockholders and have the same effect as negative votes. Proxies marked to withhold authority for all directors will not be counted in the election of directors, but will be counted for purposes of determining whether there is a quorum. On matters other than the election of directors, if a broker indicates on a proxy that it does not have discretionary authority as to certain shares to vote on a particular matter (a broker non-vote), while those shares will be included in the determination of whether a quorum is present, broker non-votes will have no effect on those matters.

REVOCABILITY OF PROXIES

Proxies which are properly executed and received by the Company before the Annual Meeting will be voted at the Annual Meeting. Any stockholder giving a proxy has the power to revoke the proxy at any time prior to its exercise. A proxy can be revoked by an instrument of revocation delivered prior to the Annual Meeting to the Secretary of the Company, by a duly executed proxy bearing a later date or time than the date or time of the proxy being revoked, or at the Annual Meeting if the stockholder is present and elects to vote in person. Mere attendance at the Annual Meeting will not serve to revoke a proxy.

SOLICITATION OF PROXIES

Solicitation of proxies may be made by directors, officers and other employees of the Company by personal interview, telephone, telegraph, telefax or electronic communications. No additional compensation will be paid for any such services. Costs of solicitation will be borne by the Company. APP will, upon request, reimburse the reasonable fees and expenses of banks, brokerage houses or other nominees or fiduciaries for forwarding proxy materials to, and obtaining authority to execute proxies from, beneficial owners for whose accounts they hold shares of Common Stock.

PROPOSAL ONE

ELECTION OF DIRECTORS

Seven (7) directors are to be elected to the Board at the Annual Meeting, each to serve for a one year term until the Annual Meeting to be held in 2007, and until his or her successor has been qualified and elected. All the nominees presently are directors of APP. It is intended that proxies received will be voted "FOR" the election of the nominees, unless marked to the contrary. The Board currently has eight (8) sitting directors, one of whom (Stephen Drury) is not standing for re-election at the Annual Meeting. In accordance with the Company's bylaws, the Board has fixed the number of directors constituting the Board of Directors at seven (7), effective just prior to the election of directors at the Annual Meeting.

The Board has no reason to believe that any of the nominees will be unable or unwilling to serve as a director if elected. If any nominee should become unavailable prior to the election, the accompanying proxy will be voted for the election of any nominee who is designated by the present Board of Directors to fill the vacancy.

INFORMATION CONCERNING THE BOARD OF DIRECTORS AND EXECUTIVE OFFICERS

The nominees for Directors of APP and their ages and position with the Company are as follows:

NAME	AGE	POSITION WITH COMPANY	DIRECTOR SINCE
Paul Goddard, Ph.D.	56	Chairman	2000
Michael O'Connell	56	President and Chief Executive Officer	2000
Peter Riepenhausen (3)(4)	69	Director	1991
Toby Rosenblatt (1)(2)(3)(4)	67	Director	1983
Gregory Turnbull (1)(2)(3)(4)	67	Director	1986
Dennis Winger (1)(2)	58	Director	1993
Robert Zerbe, M.D.	55	Director	2002

(1) Member of the Audit Committee of the Board.

- (2) Member of the Finance Committee of the Board.
- (3) Member of the Compensation and Stock Option Committee of the Board.
- (4) Member of the Nominating and Governance Committee of the Board.

The other executive officers of APP and their ages and position with the Company are as follows:

NAME	AGE	POSITION WITH COMPANY	EXECUTIVE SINCE
John Barr, Ph.D.	46	Vice President of Research and Development	1997
Gordon Sangster	53	Chief Financial Officer, Vice President of Finance	1993

Paul Goddard, Ph.D. -- chairman of A.P. Pharma board of directors since November 2000. From 1998 to 2000, Dr. Goddard was President and Chief Executive Officer of Elan's pharmaceutical division. From 1991 to 1998, Dr. Goddard served as Chairman and Chief Executive Officer of Neurex Corporation. In 1998, Neurex was acquired by Elan. Prior to Neurex, Dr. Goddard held various senior management positions at SmithKline Beecham. Dr. Goddard is Chief Executive Officer and Chairman of the Board for ARYx Therapeutics, Inc. He is also a director of Adolor, Inc., Molecular Devices, Inc. and Onyx Pharmaceuticals, Inc.

Michael O'Connell -- director since August 2000 and Chief Executive Officer and President of A.P. Pharma since August 2000; he originally joined A.P. Pharma in July 1992 as Vice President and Chief Financial Officer. From 1980 to 1992, Mr. O'Connell served with The Cooper Companies, Inc. (formerly CooperVision, Inc.) in a number of financial positions including Vice President and corporate controller. Mr. O'Connell is a Fellow of the Institute of Chartered Accountants of England and Wales.

Peter Riepenhausen -- director of A.P. Pharma since April 1991. Mr. Riepenhausen is a business consultant. He was chairman, Europe for Align Technology, Inc. from 2000 until 2002 and President and Chief Executive Officer of ReSound Corporation from 1994 to 1998. He served as a director of Caradon (Europe) plc from April 1994 until September 1998. He currently serves as Chairman of the Board of OrthoClear Inc. and as a director of Audimed GmbH and The Resource Group (TRG).

Toby Rosenblatt -- director of A.P. Pharma since September 1983. Mr. Rosenblatt is President of Founders Investments, Ltd., a private investment limited partnership. Mr. Rosenblatt also serves as a director of the BlackRock Open End Mutual Funds and is a trustee of numerous civic and educational institutions.

Gregory Turnbull -- director of A.P. Pharma since February 1986. Mr. Turnbull is currently a business consultant. Previously, he was a general partner of Cable & Howse Ventures, a venture capital firm, and also served as an investment banker with Morgan Stanley & Co. and White, Weld & Co. Mr. Turnbull serves as Chairman of the Board for Planar Systems, Inc.

Dennis Winger -- director of A.P. Pharma since February 1993. Mr. Winger is Senior Vice President and Chief Financial Officer of Applera Corporation. From 1989 to 1997, Mr. Winger was Senior Vice President, Finance and Administration and Chief Financial Officer of Chiron Corporation. He currently serves as a director of Cell Genesys and Cephalon, Inc.

Robert Zerbe, M.D. -- director of A.P. Pharma since December 2002. Dr. Zerbe is the Chief Executive Officer and founder of QuatRx Pharmaceuticals Company, a private biopharmaceutical company. Until 2000, Dr. Zerbe was employed by Pfizer as the Senior Vice President of Global Research and Development and Director of Development Operations. From 1993 to 2000, Dr. Zerbe served at the Parke-Davis Pharmaceutical Research Division of Warner-Lambert as Senior Vice President worldwide, clinical research and development. Dr. Zerbe serves as a director of Corgentech, Inc. and Aastrom Biosciences, Inc.

Executive Officers

John Barr, Ph.D. -- Vice President, Research and Development, joined A.P. Pharma in 1997 as director of Pharmaceutical Sciences. He was promoted to his current position in August 2000. Prior to joining A.P. Pharma, he worked as the director of Biopharmaceutics for Cortech, Inc. a Denver-based biotech firm

focused on the development of novel anti-inflammatory agents. In that capacity, he was involved with both the research and development aspects of the company's intravenous and oral programs. Dr. Barr received his Ph.D. in pharmacology from the University of Glasgow in Scotland, after which he pursued postdoctoral studies at the University of Arizona.

Gordon Sangster -- Chief Financial Officer, joined A.P. Pharma in 1993 as corporate controller. He became Vice President of Finance in 1994 and Chief Financial Officer in August 2000. Prior to joining A.P. Pharma, Mr. Sangster spent five years in a variety of corporate and international financial roles at Raychem, Inc. Previously, Mr. Sangster held financial positions at the Cooper Companies and at CooperVision, where he was international controller. Mr. Sangster is a member of the Institute of Chartered Accountants of England and Wales.

There are no family relationships among any of the Company's directors or executive officers.

DIRECTOR NOMINATION

Criteria for Nomination to the Board. The nominating and governance committee considers the appropriate balance of experience, skills and characteristics required of the Board of Directors, and seeks to insure that at least a majority of the directors are independent under the rules of the Nasdaq Stock Market, and that members of the Company's audit committee meet the independence and financial literacy requirements under the rules of the Nasdaq Stock Market. Nominees for director are selected on the basis of their depth and breadth of experience, integrity, ability to make independent analytical inquiries, understanding of the Company's business environment, and willingness to devote adequate time to Board duties.

Stockholder Proposals for Nominees. The nominating and governance committee will consider written proposals from stockholders for nominees for director. Any such nominations should be submitted to the nominating and governance committee c/o the Secretary of the Company and should include the following information: (a) all information relating to such nominee that is required to be disclosed pursuant to Regulation 14A under the Securities Exchange Act of 1934 (including such person's written consent to being named in the proxy statement as a nominee and to serving as a director if elected); (b) the name(s) and address(es) of the stockholder(s) making the nomination and the number of shares of the Company's Common Stock which are owned beneficially and of record by such stockholder(s); and (c) appropriate biographical information and a statement as to the qualification of the nominee. Any such nomination should be submitted no later than the date described under the caption, "Stockholder Proposals for 2007 Annual Meeting" below.

Process for Identifying and Evaluating Nominees. The process for identifying and evaluating nominees to the Board of Directors is initiated by identifying a slate of candidates who meet the criteria for selection as a nominee and have the specific qualities or skills being sought based on input from members of the Board and, if the nominating committee deems appropriate, a third-party search firm. These candidates are evaluated by the nominating committee by reviewing the candidates' biographical information and qualification and checking the candidates' references, and qualified nominees are interviewed by at least one member of the nominating and governance committee. The committee evaluates which of the prospective candidates is qualified to serve as a director and whether the committee should recommend to the Board that the Board nominate any of these final prospective candidates. Candidates recommended by the nominating and governance committee are presented to the Board for selection as nominees to be presented for the approval of the stockholders or for election to fill a vacancy.

The nominating and governance committee expects that a similar process will be used to evaluate nominees recommended by stockholders.

BOARD COMMITTEES

The Board of Directors has standing audit, finance, compensation and stock option, and nominating and governance committees.

Audit Committee. The audit committee consisted of Messrs. Drury, Rosenblatt, Turnbull (chairman) and Winger. Immediately after the Annual Meeting, the audit committee will consist of Messrs. Rosenblatt, Turnbull (chairman) and Winger. The Board has determined that all members of the audit committee are independent directors under the rules of the Nasdaq Stock Market and each of them is able to read and understand fundamental financial statements. The Board has determined that Messrs. Drury, Turnbull and Winger qualify as "audit committee financial experts" as defined by the rules of the Securities and Exchange Commission ("SEC"). The purpose of the audit committee is to oversee the accounting and financial reporting processes of the Company and audits of its financial statements. The responsibilities of the audit committee include appointing and providing the compensation of the independent accountants to

conduct the annual audit of our accounts, reviewing the scope and results of the independent audits, reviewing and evaluating internal accounting policies, and approving all professional services to be provided to the Company by its independent accountants. The audit committee operates under a written charter adopted by the Board of Directors, a copy of which was filed with the SEC as an attachment to the 2004 proxy statement.

Finance Committee. The finance committee consisted of Messrs. Drury, Rosenblatt, Turnbull (chairman) and Winger. Immediately after the Annual Meeting, the audit committee will consist of Messrs. Rosenblatt, Turnbull (chairman) and Winger. The Board has determined that all members of the finance committee are independent directors under the rules of the Nasdaq Stock Market. The finance committee is responsible for reviewing the Company's plans for providing appropriate financial resources to sustain the Company's operations including review of the Company's strategic plan and annual operating budget.

Compensation and Stock Option Committee. The compensation and stock option committee consists of Messrs. Riepenhausen, Rosenblatt (chairman) and Turnbull. The Board has determined that all members of the compensation and stock option committee are independent directors under the rules of the Nasdaq Stock Market. The compensation and stock option committee administers the Company's benefit plans, reviews and administers all compensation arrangements for executive officers, and establishes and reviews general policies relating to the compensation and benefits of our officers and employees. The compensation and stock option committee operates under a written charter adopted by the Board of Directors.

Nominating and Governance Committee. The nominating and governance committee consists of Messrs. Riepenhausen, Rosenblatt (chairman) and Turnbull, each of whom the Board has determined is an independent director under the rules of the Nasdaq Stock Market. The nominating and governance committee's responsibilities include recommending to the Board of Directors nominees for possible election to the Board of Directors and providing oversight with respect to corporate governance. The nominating and governance committee operates under a written charter adopted by the Board of Directors, a copy of which was filed with the SEC as an attachment to the 2004 proxy statement.

MEETINGS AND COMMITTEES OF THE BOARD

The Board of Directors met five times during 2005. The audit committee met five times, the finance committee met three times, the compensation and stock option committee met three times and the nominating and governance committee met once during fiscal 2005. All directors participated in at least 75% of the total number of meetings of the Board and of the committees of the Board on which each served except for Mr. Rosenblatt who attended 71% of the meetings of the Board and of the committees on which he served.

COMMUNICATIONS WITH DIRECTORS

Stockholders who wish to communicate with our Directors may do so using the procedures detailed on our website at www.appharma.com on the Corporate Governance page of the Corporate Overview section.

The Company encourages its directors to attend its annual meetings. Seven directors attended the Company's 2005 Annual Meeting.

COMPENSATION COMMITTEE INTERLOCKS AND INSIDER PARTICIPATION

No interlocking relationship exists, or in the past fiscal year has existed, between any member of our compensation committee and any member of any other company's board of directors or compensation committee.

COMPENSATION OF DIRECTORS

Each nonemployee director of the Company annually has been granted an option to acquire 10,000 shares of Common Stock, under the Company's 1992 and 2002 Stock Option Plans. In May 2005, the Company granted each of the non-employee directors an option to purchase 10,000 shares of common stock at an exercise price of \$1.60 per share. These options will be fully vested and exercisable one year from the date of grant. In addition, each nonemployee director elected after the Company's initial public offering in 1987 received a one-time grant to acquire 25,000 shares when first elected as a director. Non-employee directors of the Company also receive \$12,000 per year, \$1,000 for each meeting of the Board of Directors attended and \$500 for each committee meeting attended on a date other than the date of a regularly scheduled Board or other committee meeting. Since July 1, 2000, all compensation is payable in restricted Common Stock of the Company valued at the closing price of the Company's Common Stock on the last trading date of each quarter.

During 2005, consulting fees totaling \$4,200 were paid to Dr. Robert Zerbe.

Section 16(a) of the Securities Exchange Act of 1934 requires the Company's officers and directors, as well as any holders of more than 10% of the Company's Common Stock, to file with the SEC certain reports of ownership and reports of changes in ownership of Common Stock and other equity securities of the Company. Based solely on review of such reports and certain representations furnished to it, the Company believes that during the fiscal year ended December 31, 2005, all Section 16(a) filing requirements applicable to its officers and directors were satisfied.

COMMON STOCK OWNERSHIP OF CERTAIN BENEFICIAL
OWNERS AND MANAGEMENT

The following table sets forth beneficial Common Stock ownership as of April 5, 2006, by (i) each person who is known by the Company to own beneficially more than 5% of the outstanding shares of Common Stock, (ii) each director, including nominees, and each executive officer named in the Summary Compensation Table included in the Proxy Statement, and (iii) all executive officers and directors as a group. Each person has sole investment and voting power with respect to the shares indicated, subject to community property laws where applicable and except as otherwise set forth in the footnotes to the table. Unless otherwise indicated, the address of each of the named individuals is c/o A.P. Pharma, Inc., 123 Saginaw Drive, Redwood City, CA 94063.

NAME	NUMBER OF SHARES(1)	PERCENT OF CLASS(1)
John Barr, Ph.D.(2)	228,115	*
Stephen Drury(3)	164,854	*
Paul Goddard, Ph.D.(4)	375,000	1.5
Michael O'Connell(5)	686,850	2.7
Peter Riepenhausen(6)	239,638	*
Toby Rosenblatt(7)	340,981	1.3
Gordon Sangster(8)	188,121	*
Gregory Turnbull(9)	205,007	*
Dennis Winger(10)	150,044	*
Robert Zerbe, M.D.(11)	70,594	*
Great Point Partners, LLC(12) 2 Pickwick Plaza, Suite 450 Greenwich, CT 06830	1,992,954	7.9
North Sound Capital LLC(13) 20 Horseneck Lane Greenwich, CT 06830	2,325,934	9.2
Officers and Directors as a group(10 persons) (2)(3)(4)(5)(6)(7)(8)(9)(10)(11)	2,649,204	10.5

* Less than one percent.

- (1) Assumes the exercise of all outstanding options to purchase Common Stock held by such person or group to the extent exercisable on or before June 5, 2006, and that no other person has exercised any outstanding stock options.
- (2) Includes 170,469 shares underlying exercisable stock options and 25,000 shares of restricted stock subject to the right of repurchase which lapses on March 23, 2009.
- (3) Includes 76,586 shares held in family trust and 85,000 shares underlying exercisable stock options.
- (4) Includes 310,000 shares underlying exercisable stock options.
- (5) Includes 531,249 shares underlying exercisable stock options and 50,000 shares of restricted stock subject to the right of repurchase which lapses on March 23, 2009.
- (6) Includes 157,754 shares held in family trust and 60,000 shares underlying exercisable stock options.
- (7) Includes 160,000 shares held in family partnership and 90,000 shares underlying exercisable stock options.
- (8) Includes 182,969 shares underlying exercisable stock options.
- (9) Includes 90,000 shares underlying exercisable stock options.
- (10) Includes 90,000 shares underlying exercisable stock options.
- (11) Includes 38,750 shares underlying exercisable stock options.
- (12) Based solely on information contained in a Schedule 13G dated February 13, 2006.
- (13) Based solely on information contained in a Schedule 13G dated February 13, 2006.

EXECUTIVE COMPENSATION

The following Summary Compensation Table shows the total compensation for fiscal years 2005, 2004 and 2003 of the Chief Executive Officer and the other most highly compensated executive officers whose salary exceeded \$100,000 in 2005.

SUMMARY COMPENSATION TABLE

NAME AND POSITION	YEAR	ANNUAL COMPENSATION		LONG-TERM COMPENSATION AWARDS		
		SALARY (\$)	BONUS (\$)	RESTRICTED STOCK AWARDS (\$)(1)	SECURITIES UNDERLYING OPTIONS (#)	ALL OTHER COMPENSATION (\$)
Michael O'Connell President and Chief Executive Officer	2005	326,308	91,366	84,500	--	6,300(2)
	2004	320,000	36,389	--	50,000	6,150(2)
	2003	313,269	32,893	--	40,000	6,000(2)
John Barr, Ph.D. Vice President, Research and Development	2005	219,623	61,494	42,250	--	6,300(2)
	2004	213,000	24,221	--	25,000	6,150(2)
	2003	207,615	21,800	--	7,500	4,332(2)
Gordon Sangster Chief Financial Officer, Vice President of Finance	2005	204,500	49,080	--	--	6,135(2)
	2004	204,500	19,933	--	--	6,135(2)
	2003	204,500	18,405	--	7,500	6,000(2)

(1) The dollar value of restricted stock awards, net of consideration paid by the named executive officer, was calculated using the closing market price of the Company's Common Stock on the date the restricted stock award was granted. Each restricted stock award provides that for a period of four years after the award of restricted stock, the recipient may not sell, assign, transfer, pledge or otherwise encumber the shares of restricted stock. Any cash dividends with respect to shares of restricted stock are automatically reinvested in additional shares of restricted stock. Each restricted stock award provides that if the employee should leave the employ of the Company prior to four years from the date of award, unless waived by the administrator of the plan under certain circumstances, the Company will have the right to repurchase the restricted stock at their original purchase price of \$.01 per share. As of December 31, 2005, the Company had a total of 75,000 shares of restricted stock outstanding with an aggregate value of \$114,750 based on the value of the Company's shares at December 31, 2005.

(2) The stated amounts are Company matching contributions to the A.P. Pharma 401K Plan. The Company made matching cash contributions equal to 50% of each participant's contribution during the plan year up to a maximum amount equal to the lesser of 3% of each participant's annual compensation or \$6,300, \$6,150 and \$6,000 for the years 2005, 2004 and 2003, respectively.

No stock options were granted to executives during 2005.

The following table sets forth certain information with respect to the value of options held at fiscal year-end by the executive officers named in the Summary Compensation Table. No options were exercised during 2005 by any of the named executive officers.

AGGREGATED 2005 YEAR-END OPTION VALUES

NAME	NUMBER OF UNEXERCISED OPTIONS AT 2005 YEAR-END		VALUE OF UNEXERCISED IN-THE-MONEY OPTIONS AT FISCAL YEAR-END (1)	
	EXERCISABLE (#)	UNEXERCISABLE (#)	EXERCISABLE (\$)	UNEXERCISABLE (\$)
Michael O'Connell	513,958	41,042	13,417	4,983

John Barr, Ph.D.	162,865	17,135	3,453	1,122
Gordon Sangster	180,886	4,114	3,453	1,122

(1) Market value of underlying securities at fiscal year-end minus the exercise price of "in-the-money" options.

REPORT OF THE COMPENSATION AND STOCK OPTION COMMITTEE

The Compensation and Stock Option Committee of the Board of Directors (the "Committee") is responsible for establishing compensation policies applicable to the Company's executive officers and, pursuant to such policies, determining the compensation payable to the Company's Chief Executive Officer and other executive officers of the Company. The Committee consists of Peter Riepenhausen, Toby Rosenblatt and Greg Turnbull, each of whom is a non-employee director of the Company and independent under the Nasdaq Stock Market rules. In determining compensation policies, the Committee has access to compensation surveys for companies which compete with the Company in the recruitment and retention of senior executives as well as other executive compensation information and data. The following report relates to compensation payable to the Company's executive officers for the year ended December 31, 2005.

COMPONENTS OF COMPENSATION

There are three components of compensation payable to the Company's executive officers: base salary, equity-based incentive compensation in the form of stock options and restricted stock awards and annual incentive compensation in the form of cash bonuses.

COMPENSATION POLICIES

The Company's compensation policies for all employees, including executive officers, are designed to provide targeted compensation levels that are competitive with those of companies of similar size, with whom the Company must compete in the recruitment of senior personnel. The Committee also seeks to tie incentive cash bonuses to the achievement of pre-established performance objectives for the Company approved by the Committee and the Board of Directors, and to use equity-based compensation to promote equity-ownership in the Company at levels deemed appropriate by the Committee for executive officers and employees. The goals of the Committee are to align compensation with the Company's objectives and performance, and to enable the Company to attract, retain and reward executives and employees who contribute to the long-term success of the Company. The Company does not believe that compensation payable by it will be subject to the limitations on deductibility provided under Section 162(m) of the Internal Revenue Code.

BASE SALARIES

The salary component of executive compensation is based on the executive's level of responsibility for meeting the Company's objectives and performance, and comparison to similar positions in the Company and comparable companies. Base salaries for executive officers are reviewed and adjusted annually based on information regarding competitive salaries, including salary survey data provided by third parties. Individual increases are established by the Committee (taking into account recommendations of the chief executive officer concerning the overall effectiveness of each executive).

CASH BONUSES

Cash bonuses for executive officers and all other employees are determined under the Company's management by objectives program ("MBO") which is approved annually by the Board of Directors. The MBO plan establishes annual corporate goals and a target bonus for all employees, including each executive officer, which is a percentage of base salary. The purpose of the plan is to facilitate the company's development and commercialization of its product pipeline and to translate business goals into individual accountabilities by linking performance to compensation. The percentage of the target bonus that is paid to each officer is dependent upon the percentage achievement of corporate goals. Achievement of corporate goals is determined at the end of the year and approved by the Compensation Committee. Related bonuses are paid in the subsequent year. Bonuses earned by the executive officers for achieving a percentage of the 2005 corporate goals were paid in January 2006.

EQUITY AWARDS

The Company's compensation policies recognize the importance of stock ownership by senior executives and equity-based incentive compensation is an integral part of each executive's compensation. The Committee believes that the opportunity for stock appreciation through stock options which vest over

time promotes the relationship between long-term interests of executive officers and stockholders. The size of specific options grants takes into account the executive officer's salary, number of options previously granted, as well as shares of Common Stock held, and the contributions to the Company's success.

The Company's 2002 Equity Incentive Plan permits the awards of restricted stock. Restricted stock awards were granted to two executive officers in 2005.

COMPENSATION PAYABLE TO CHIEF EXECUTIVE OFFICER

The 2005 salary for Mr. O'Connell, the Company's President and Chief Executive Officer, was determined principally by evaluating his performance in his leadership role in the Company and his contributions in executing the strategic and operating plan of the Company and taking into consideration competitive compensation levels for comparable companies. The Compensation Committee and Board of Directors decided to increase his base salary from \$320,000 to \$340,000 effective September 1, 2005. In 2005, the Compensation Committee and Board of Directors approved the grant to Mr. O'Connell of a restricted stock award of 50,000 shares. As of April 5, 2006, Mr. O'Connell held presently exercisable stock options to purchase 525,626 shares and, including options, beneficially owns as of that date 681,227 shares of the Company's Common Stock.

Compensation and Stock Option Committee
Peter Riepenhausen
Toby Rosenblatt
Gregory Turnbull

INDEMNIFICATION AGREEMENTS

We have entered into indemnification agreements with our directors and executive officers. Such agreements require us, among other things, to indemnify our officers and directors, other than for liabilities arising from willful misconduct of a culpable nature, and to advance their expenses incurred as a result of any proceedings against them as to which they could be indemnified.

REPORT OF THE AUDIT COMMITTEE

The Audit Committee of the Board of Directors is comprised solely of independent directors as defined under the listing standards of the Nasdaq Stock Market and operates under a written charter adopted by the Board of Directors. The Audit Committee, on behalf of the Board of the Directors, provides general oversight of the Company's financial accounting and reporting process, including the system of internal control. The Audit Committee also oversees and evaluates the performance of the Company's independent auditors and provides an open avenue of communication among the independent auditors, financial and senior management and the Board of Directors.

The Company's management has primary responsibility for preparing the Company's financial statements and for the Company's financial reporting process including the system of internal control. The Company's independent auditors are responsible for expressing an opinion on the conformity of the Company's audited financial statements to accounting principles generally accepted in the United States of America.

In this context and in connection with the audited financial statements contained in the Company's 2005 Annual Report on Form 10-K, the Audit Committee:

* reviewed the audited financial statements with the Company's management, including a discussion of the quality of the accounting principles. In addition, the Committee met with management and the Company's auditors on a quarterly basis, to review the quarterly financial statements prior to their release;

* discussed with the Company's independent auditors, their judgment as to the quality of the Company's accounting principles, as well as certain matters related to the conduct of the audit, as required by Statement of Auditing Standards No. 61, as amended by Statement on Auditing Standards No. 90, Communication with Audit Committees;

* met with the independent auditors, with and without management present, to discuss the results of their audit and the overall quality of the Company's financial reporting;

* reviewed the written disclosures and the letter from the independent auditors required by Independence Standard Board Standard No. 1, "Independence Discussions with Audit Committees," and discussed with the auditors their independence from the Company, and concluded that the non-

audit services performed by the independent auditors are compatible with maintaining their independence;

* instructed the independent auditors that the Committee expects to be advised if there are any subjects that require special attention.

Based on the review and discussions described above, the Audit Committee recommended to the Board of Directors that the Company's audited consolidated financial statements for the fiscal year ended December 31, 2005 be included in the Company's Annual Report on Form 10-K for the year ended December 31, 2005, for filing with the SEC, and the Board of Directors approved such inclusion. The Audit Committee has also selected Odenberg, Ullakko, Muranishi & Co., LLP as the Company's independent registered public accountants to audit the financial statements of the Company for the fiscal year ending December 31, 2006, subject to stockholder ratification. A representative from Ernst & Young, LLP will be present at the Annual Meeting to answer any questions relating to the audit of the financial statements for the fiscal year ending December 31, 2005.

Audit Committee
Stephen Drury
Toby Rosenblatt
Gregory Turnbull
Dennis Winger

AUDITOR FEES AND SERVICES

The aggregate fees paid for professional services relating to fiscal 2005 and 2004 for each of the following categories of services are as follows:

	2005	2004
	----	----
Audit fees(1)	\$312,996	\$303,717
Tax fees(2)	23,800	20,800
All other fees	19,800	16,300

- - - - -
- (1) Audit fees include fees for the audit of our consolidated financial statements and interim reviews of our quarterly financial statements and consents. Audit-related fees for 2004 include the audit of (a) management's assessment of internal control over financial reporting and (b) the effectiveness of internal control over financial reporting, as required under Section 404 of the Sarbanes-Oxley Act of 2002.
- (2) Tax fees consist of fees for tax compliance and tax advice.

The Board has delegated to the Audit Committee the authority to pre-approve audit-related and non-audit services not prohibited by law to be performed by the Company's independent auditors and associated fees, provided that the Audit Committee shall report any decision to pre-approve such audit-related or non-audit services and fees to the full Board at its next regular meeting.

The Audit Committee has delegated to the Chair of the Audit Committee the authority to pre-approve audit-related and non-audit services not prohibited by law to be performed by the Company's independent auditors and associated fees up to a maximum of \$25,000 during 2006, provided that the Chair shall report any decision to pre-approve such audit-related or non-audit services and fees to the full Audit Committee at its next regular meeting.

PERFORMANCE GRAPH

The rules of the SEC require APP to include in this Proxy Statement a line graph presentation comparing cumulative five year stockholder returns, on a dividend reinvested basis, with a broad based equity index and a published industry index. The Company selected the S&P 500 Stock Index and Russell 2000 for purposes of the comparison which appears below. The graph assumes that \$100 was invested in APP stock and each index on December 31, 2000, with all dividends reinvested. Past stock performance is not necessarily indicative of future results.

[The following descriptive data is supplied in accordance with Rule 304(d) of Regulation S-T]

	12/00	12/01	12/02	12/03	12/04	12/05
	-----	-----	-----	-----	-----	-----
A.P. PHARMA, INC.	100	118	42	103	69	64
S&P 500	100	88	69	88	98	103
RUSSELL 2000	100	102	81	120	142	148

CERTAIN TRANSACTIONS

In 2000, the Company approved a Retention Incentive Plan ("Retention Plan") for Mr. O'Connell. The purpose of the Retention Plan was to encourage Mr. O'Connell to continue his employment with the Company, enhance his ability to perform effectively and provide the Company with the benefit of his continued service. Under the Retention Plan, the Company entered into a retention agreement with Mr. O'Connell providing that he will be eligible for certain benefits if his employment is terminated under specified circumstances. If Mr. O'Connell's full-time employment with the Company is terminated by the Company (other than for cause) or by the executive for good reason (due to material reduction in the executive's authority or responsibility, base salary or other compensation or employee benefits), he will be retained as a part-time employee for a period of 24 months (the "Retention Period"). During the Retention Period, Mr. O'Connell will receive continuation of salary, payable one-half in a lump sum following termination of full-time employment and the remainder ratably over the Retention Period and an annual bonus equal to the bonus paid during the immediately preceding 12-month period. On March 23, 2005, the Board of Directors approved an amendment to its Retention and Non-Competition Agreement with Mr. O'Connell. The principal changes to Mr. O'Connell resulting from the amendment include adding (a) full accelerated vesting of options granted to him should his employment be terminated by the Company without cause or by him for good reason after a change of control and (b) the lapse of restrictions on restricted stock held by him upon a change of control.

In 2000, the Company approved an agreement with Dr. Goddard under which he received a stock option grant to acquire 75,000 shares of the Company's Common Stock. Twenty-five percent of the options vested at the end of twelve months and the balance vests in equal monthly installments for the next 36 months. The agreement provided that Dr. Goddard would receive additional option grants each year of 20,000 shares while he serves as chairman.

In September 2004, Dr. Goddard entered into an additional agreement with the Company to increase his involvement in the Company's activities. As compensation for his increased involvement, he received a stock option grant in September 2004 to acquire 120,000 shares of the Company's Common Stock. The option will vest 25% after the first year and then monthly over a period of three years and fully vest on September 15, 2008. Under this new agreement, he is not entitled to receive the additional annual option grants of 20,000 shares for the years 2005 and 2006. Additionally, effective March 6, 2005, Dr. Goddard's cash compensation was reduced to \$150,000. On August 23, 2005, Dr. Goddard's existing agreement was modified to reflect his reduced schedule. He no longer receives an annual salary and instead is compensated on a per diem basis for services performed.

On November 1, 2003, the Company entered into a Change of Control Agreement with Dr. Barr which provides that if his employment is terminated by the Company without good cause within 12 months after a change of control of the Company, he will receive for a period of 12 months, his base salary together with an average of any bonus paid during each of the three 12-month periods prior to termination, payable in 12 equal monthly installments.

On March 23, 2005, the Board of Directors approved an amendment to its Change of Control Agreement with Dr. Barr. The principal changes to Dr. Barr resulting from the amendment include adding (a) full accelerated vesting of options granted to him should his employment be terminated by the Company without cause or by him for good reason after a change of control and (b) the lapse of restrictions on restricted stock held by him upon a change of control. Mr. Barr's agreement expires on December 31, 2006.

Also on March 23, 2005, the Board of Directors approved a Change of Control Agreement for Mr. Sangster, Chief Financial Officer. Mr. Sangster's Agreement provides that if his employment is terminated by the Company without good cause within 12 months after a change of control of the Company, he will receive (a) for a period of 12 months, his base salary together with an average of any bonus paid during each of the three 12-month periods prior to termination, payable in 12 equal monthly installments, and (b) full accelerated vesting of options granted to him prior to termination without good cause or by him for good reason following a change of control. Mr. Sangster's agreement expired on December 31, 2005.

AMENDMENT TO THE 1997 EMPLOYEE STOCK PURCHASE PLAN

The Board of Directors has approved an amendment, subject to stockholder approval, to the 1997 Employee Stock Purchase Plan ("Purchase Plan"). The following description of the Purchase Plan is a summary and so qualified by reference to the complete text of the Purchase Plan. The Purchase Plan permits the Company's employees to purchase the Company's Common Stock at a discounted price. This plan is designed to encourage and assist employees of the Company to acquire an equity interest in the Company through the purchase of shares of Company Common Stock. Approximately 33 employees of the Company are eligible to participate in the Purchase Plan. You can request a copy of the 1997 Employee Stock Purchase Plan by writing to the Company to the attention of Marea Fabrique, Investor Relations.

Subject to stockholder approval, the Board of Directors has approved an increase of 150,000 shares from 650,000 to 800,000 shares, under the Purchase Plan. Management expects these shares to be sufficient for all stock purchases under the plan for approximately three years. As of March 31, 2006, 511,918 shares have been issued under the Purchase Plan.

DESCRIPTION OF THE PURCHASE PLAN

All employees, including executive officers, customarily employed more than 20 hours per week and more than five months per year by the Company are eligible to participate in the Employee Stock Purchase Plan as of the first semi-annual enrollment date following employment. However, employees who hold, directly or through options, five percent or more of the stock of the Company are not eligible to participate. Participants may elect to make contributions up to a maximum of 10% of base earnings. On the last trading date of April and October, the Company applies the funds then in each participant's account to the purchase of shares. The cost of each share purchased is 85% of the lower of the closing prices for Common Stock on: (i) the first trading day in the enrollment period in which the purchase is made; and (ii) the purchase date. The length of the enrollment period may not exceed a maximum of 24 months. Enrollment dates are the first business day of May and November. The Board may limit the maximum number of shares that may be purchased by a participant during any enrollment period, and no participant's right to acquire shares may accrue at a rate exceeding \$25,000 of fair market value of Common Stock (determined as the lower of the fair market value on the first trading day in an enrollment period or the fair market value on the purchase date) in any calendar year.

The Board of Directors may administer the Purchase Plan or the Board may delegate its authority to a committee of the Board. The Board of Directors may amend or terminate the Purchase Plan at any time and may provide for an adjustment in the purchase price and the number and kind of securities available under the plan in the event of a reorganization, recapitalization, stock split, or other similar event. However, amendments that would increase the number of shares reserved for purchase, or would otherwise require stockholder approval in order to comply with certain federal tax laws, require stockholder approval. Shares available under the plan may be either outstanding shares repurchased by the Company or newly issued shares.

The following table shows the "Dollar Value" and number of shares applicable to the named individuals and groups under the Purchase Plan during the year ended December 31, 2005, purchased on the April and October 2005 purchase dates under the Purchase Plan at a purchase price of \$1.10 and \$1.42, respectively. These amounts represent 85% of the closing price on the first trading date of the enrollment period of May, 2003, November, 2004 or May, 2005. The "Dollar Value" is the difference between the fair market value of the Common Stock on the purchase date of April 29, 2005 or October 31, 2005 and the participant's purchase price of \$1.10 or \$1.42 per share.

Since purchase rights are subject to discretion, including an employee's decision not to participate in the Purchase Plan, awards under the Purchase Plan for the current fiscal year are not determinable. No purchase rights have been granted with respect to the additional 150,000 shares for which approval is requested.

PLAN BENEFITS
1997 EMPLOYEE STOCK PURCHASE PLAN

Name and Position - - - - -	Dollar Value (\$) - - - - -	Number of Shares - - - - -
Michael O'Connell President and Chief Executive Officer	14,526	23,401

John Barr, Ph.D.
Vice President, Research and Development

3,649

5,874

Executive Officers as a Group
Non-Executive Officer Employee Group

18,175
34,188

29,275
57,174

FEDERAL INCOME TAX CONSEQUENCES

The following general description of federal income tax consequences is based upon current statutes, regulations and interpretations thereof. Because the applicable rules are complex and because income tax consequences may vary depending upon the individual circumstances of each participant, participants should consult their personal tax advisors concerning federal, state, local and foreign income tax consequences associated with their participation in the Purchase Plan.

In general, participants will not have taxable income or loss under the Purchase Plan until they sell or otherwise dispose of shares acquired under the plan (or die holding such shares). If the shares are held, as of the date of sale or disposition, for longer than both: (i) two years after the beginning of the enrollment period during which the shares were purchased; and (ii) one year following purchase, a participant will have taxable ordinary income equal to 15% of the fair market value of the shares on the first day of the enrollment period (but not in excess of the fair market value of the shares at the time of sale over the purchase price). Any additional gain (or loss) from the sale will be long-term capital gain (or loss). The Company is not entitled to an income tax deduction if the holding periods are satisfied.

If the shares are sold or disposed of before the expiration of either of the foregoing holding periods (a "disqualifying disposition"), a participant will have taxable ordinary income equal to the excess of the fair market value of the shares on the purchase date over the purchase price. In addition, the participant will have a taxable capital gain (or loss) measured by the difference between the sale price and the participant's purchase price which gain (or loss) will be long-term if the shares have been held as of the date of sale for more than one year. The Company is entitled to an income tax deduction equal to the amount of ordinary income recognized by a participant in a disqualifying disposition.

PROPOSAL

At the Annual Meeting, the Company's stockholders will be asked to approve the increase to the 1997 Employee Stock Purchase Plan. Such approval will require the affirmative vote of a majority of the shares present and voting at the Annual Meeting. The Board of Directors recommends a vote "FOR" the proposal.

PROPOSAL THREE

AMENDMENT TO THE COMPANY'S 2002 EQUITY INCENTIVE PLAN

The Company's 2002 Equity Incentive Plan is intended to strengthen the Company by providing added incentive to officers, directors, employees and consultants for high levels of performance and unusual efforts to increase the earnings of the Company through the opportunity for stock ownership. Subject to stockholder approval, the Board has approved to increase by 400,000 shares the number of shares of Common Stock reserved for issuance under the Plan. The following description of the 2002 Equity Incentive Plan is a summary and so qualified by reference to the complete text of the purchase plan. You can request a copy of the 2002 Equity Incentive Plan by writing to the Company to the attention of Marea Fabrique, Investor Relations.

The Board of Directors believes it would be in the best interest of the Company to approve the amendment to the 2002 Equity Incentive Plan to increase the number of shares by 400,000. The 2002 Equity Incentive Plan, currently the only plan pursuant to which the Company grants options, has only 238,700 shares available for grant as of April 5, 2006. As a consequence, without approval of an increase in the number of shares of Common Stock reserved for issuance under the 2002 Equity Incentive Plan, the Company anticipates it will no longer have shares available for grant after 2006. The grant of stock options or restricted stock has been an important component of the compensation of Company directors, officers and other key employees and an important means of providing an opportunity for stock ownership to such personnel. As of March 31, 2006, directors, officers, employees and consultants held unexercised options under the 2002 Equity Incentive Plan covering 936,566 shares of Common Stock with an average exercise price of \$1.72.

DESCRIPTION OF THE 2002 EQUITY INCENTIVE PLAN

The following is a general summary of the principal provisions of the 2002 Equity Incentive Plan. The 2002 Equity Incentive Plan authorizes the granting of Incentive Stock Options ("ISOs") to employees (including employees who are

officers and directors) and Nonstatutory Options ("NSOs") to officers, directors, employees and consultants to purchase authorized, but unissued shares of the Company's Common Stock. The 2002 Equity Incentive Plan also provides for grants of restricted stock awards and, subject to stockholder approval the number of shares reserved for issuance under the 2002 Equity Incentive Plan will be 1,700,000. The 2002 Equity Incentive Plan is administered by the Administrator which determines the terms of options granted under the 2002 Equity Incentive Plan, including the exercise price, number of shares subject to the option, whether the option is an ISO or an NSO, and the schedule pursuant to which the option shall become exercisable. No option may be granted under the 2002 Equity Incentive Plan after April, 2012, but outstanding options may extend beyond that date.

The Company pays directors for services in Company stock, and uses NSOs as a way to compensate non-employee directors and to provide incentives to them through an equity interest in the Company. A 10 year NSO to purchase 25,000 shares of the Company's Common Stock will be granted to each person who is neither an officer nor an employee of the Company when such person is first elected or appointed director. Each such option vests at the rate of 25% per year, so long as the individual is serving as a director, with full vesting over four years. A non-employee director also receives a grant of a ten year NSO to purchase 10,000 shares of Common Stock on the date of each annual meeting of stockholders of the Company held more than 12 months after a non-employee director is first elected or appointed to the Board of Directors. These options fully vest one year after the date of grant.

The exercise price of each option granted under the 2002 Equity Incentive Plan must be at least equal to 100% of the fair market value of the underlying shares of Common Stock on the date of grant. The 2002 Equity Incentive Plan provides that the maximum term of an option is ten years. With respect to any participant then owning stock possessing more than ten percent (10%) of the voting power of the Company's outstanding capital stock, the exercise price of any ISO must be at least 110% of fair market value of the underlying shares of Common Stock on the date of grant, and the term may be no longer than five years. The 2002 Equity Incentive Plan permits the exercise of options for cash, a check, or with the approval of the Administrator, tender to the Company of shares of the Company's Common Stock owned by the optionee and having a fair market value not less than the option exercise price or delivery of full recourse promissory notes.

The 2002 Equity Incentive Plan limits to \$100,000 the value of option stock (measured at the time of the option grant) with respect to which ISOs granted to any one employee after 1986 under any Company plan may vest in any calendar year. Furthermore, no optionee may be granted one or more options to purchase more than 250,000 shares within any fiscal year of the Company (the "162(m) Share Limit").

At the time an option is exercised, in whole or in part, or at any time thereafter as requested by the Company, the optionee is required to make adequate provision for federal and state income and employment tax withholding obligations of the Company, if any, resulting from the exercise. Subject to certain limitations, an optionee may elect, subject to the terms of the 2002 Equity Incentive Plan and the approval of the Administrator, to have shares of Common Stock issuable on exercise of the options withheld or to tender shares then owned by the optionee to provide for these taxes.

Generally, options are exercisable not upon grant, but in cumulative increments over time, typically 25% per year over four years. Options may be exercised for ninety days after the optionee leaves the Company and, if the optionee's employment is terminated by reason of death or permanent disability, for one year after the optionee's death or disability, but in either case not beyond the original term of the option.

In the event of a merger of the Company, sale of substantially all of its assets or similar transaction, the Administrator may, among other things, accelerate the expiration date and the exercisability of all options outstanding under the 2002 Equity Incentive Plan.

Under the 2002 Equity Incentive Plan, the Administrator also may grant to participants a direct right to purchase shares by notifying the grantee of the terms, conditions and restrictions relating to the purchase right.

The 2002 Equity Incentive Plan also provides for the grants of restricted stock awards. A restricted stock award is an award of shares of Common Stock which are subject to restrictions on transfer for a period of time specified by the Administrator (the "Restriction Period") provided, that the Restriction Period may not exceed 10 years and may not be less than three years. During the Restriction Period, the recipient of the restricted stock award may not sell, assign, transfer, pledge or otherwise encumber shares of restricted stock. Within these limits, the Administrator may provide for the lapse of such restrictions in installments, but other than in the case of acquisition of the Company, may not waive or accelerate the restrictions.

The recipient of the restricted stock award must pay a purchase price determined by the Administrator, which shall not be less than the par value (\$.01 per share) for all shares of restricted stock awarded. In the event the holder of the restricted stock ceases to be employed by (or to act as a director of or consultant to) the Company prior to the end of the Restriction Period, all shares still subject to restriction are forfeited and repurchased by the Company for the price paid by the participant. Before the Restriction Period expires, unless otherwise determined by the Administrator, cash dividends, if any with respect to the restricted stock awards will be automatically reinvested in additional restricted stock, and dividends payable in stock will be in the form of restricted stock. Any restricted stock awards intended as "qualified performance-based compensation" within the meaning of Section 162(m) of the Code must vest or become exercisable contingent on the achievement of one or more objectively determinable performance conditions approved by the stockholders of the Company.

The 2002 Plan expires in April, 2012, unless terminated earlier by the Board of Directors. The Board may at any time terminate or amend the 2002 Equity Incentive Plan, provided that without approval of stockholders there will be no increase in the total number of shares covered by the 2002 Equity Incentive Plan. In any case, no amendment may adversely affect any then-outstanding option or unexercised portion thereof without the optionee's consent unless such amendment is required to enable the option to qualify as an ISO.

The following table shows the number of options granted to the named individuals and groups under the 2002 Equity Incentive Plan during 2005.

Because the grants under the 2002 Equity Incentive Plan are discretionary, benefits for the current fiscal year are not determinable. No awards have been granted with respect to the additional 400,000 shares for which approval is requested.

PLAN BENEFITS
2002 EQUITY INCENTIVE PLAN

Name and Position - - - - -	Number of Options (1) - - - - -
Michael O'Connell President and Chief Executive Officer	50,000(2)
John Barr, Ph.D. Vice President, Research and Development	25,000(2)
Executive Officers as a Group	75,000
Non-Executive Director Group	60,000
Non-Executive Officer Employee Group	112,000

- - - - -
- (1) All options granted at fair market value on the date of the grant.
 - (2) Restricted stock award granted.

FEDERAL INCOME TAX CONSEQUENCES OF STOCK AWARDS

The following general description of federal income tax consequences is based upon current statutes, regulations and interpretations thereof. Because the applicable rules are complex and because income tax consequences may vary depending upon the individual circumstances of each participant, participants should consult their personal tax advisors concerning federal, state, local and foreign income tax consequences associated with their participation in the 2002 Equity Incentive Plan.

ISOs granted under the 2002 Equity Incentive Plan are intended to constitute "incentive stock options" within the meaning of the Section 422 of the Code. ISOs may be granted only to employees of the Company (including directors who are also employees). An optionee does not recognize taxable income upon either the grant or exercise of an ISO. However, the excess of the fair market value of the shares purchased upon exercise over the option exercise price (the "Option Spread") is includible in the optionee's "alternative minimum tax income" ("AMTI"), used to calculate the "alternative minimum tax". The Option Spread is measured on the date of exercise and is generally includible in AMTI in the year of exercise.

If an optionee holds shares which result from the exercise of an ISO for at least two years from the date the ISO was granted, and for at least one year from the date the ISO was exercised, any gain from a sale of the shares should be taxable as long-term capital gain. Under these circumstances, the Company

would not be entitled to a tax deduction at the time the ISO is exercised or at the time the stock is sold. If an optionee were to dispose of stock acquired pursuant to an ISO before the end of the required holding periods (a "Disqualifying Disposition"), the amount by which the market value of the stock at the time the ISO was exercised exceeds the exercise price (or, if less, the amount of gain realized on the sale) would be taxable as ordinary income, and the Company should be entitled to a corresponding tax deduction. A gain recognized in connection with a Disqualifying Disposition, in excess of the amount required to be recognized as ordinary income would be a capital gain (which will be long-term capital gain if the shares have been held more than one year after the date of exercise of the option). If the sale price is less than the exercise price in a Disqualifying Disposition, the optionee would recognize a capital loss equal to the difference between the exercise price and the sale price.

An optionee is not taxed upon the grant of an NSO. Generally, the optionee will recognize as ordinary income the Option Spread on the date of exercise. The Company is entitled to a deduction equal to the amount of ordinary income recognized by an optionee who is an employee and such income recognized by an employee is subject to income tax withholding by the Company. Upon the disposition of stock acquired upon exercise of an NSO, an optionee will recognize either long-term or short-term capital gain or loss, depending on how long such stock was held, on any difference between the sale price and the exercise price, to the extent not recognized as taxable income on the date of exercise.

In the case of both ISOs and NSOs, special federal income tax rules apply if Company common stock is used to pay all or part of the option exercise price, and different rules than those described above will apply if unvested shares are purchased on exercise of the option.

Generally, a participant should not have taxable income upon the grant of restricted stock but would have taxable income upon the lapse of any restrictions in an amount equal to the difference between the fair market value of the restricted stock when the restrictions lapse and the amount paid for the restricted stock, if any. A participant receiving restricted stock may, however, make an election pursuant to Section 83(b) of the Code (within 30 days of grant of the restricted stock) to be taxed at grant on any excess of fair market value over the amount paid, in which case the lapse of any restrictions will not be a taxable event. If shares are held at least one year after the date the optionee recognizes taxable income with respect to such shares, or from filing an 83(b) election with respect to the shares, then upon sale of the shares the employee will have long-term capital gain or loss equal to the difference between the sale price and the fair market value of the shares of the date income is recognized. The Company is entitled to a deduction in the same amount and at the time as the participant recognizes ordinary income.

EQUITY COMPENSATION PLAN INFORMATION

The table below discloses the following information as of December 31, 2005 with respect to A.P. Pharma's equity compensation plans that have been approved by stockholders and plans that have not been approved by stockholders.

Plan Category	(a) Number of securities to be issued upon exercise of outstanding options	(b) Weighted-average exercise price of outstanding options	(c) Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a))
Equity compensation plans approved by security holders	2,023,466	\$3.50	442,700
Equity plans not approved by security holders	142,500	2.01	96,041
Total	2,165,966	3.40	538,741

In October 2000, the Company adopted the Non-Qualified Stock Plan, which has not been approved by A.P. Pharma's stockholders. The Non-Qualified Stock Plan will expire in 2010. Under the Non-Qualified Stock Plan, awards may be granted as a material inducement to any person accepting employment or consultancy with the Company or an employee of the Company who is not an officer or director of the Company at the time of the award. The Non-

Qualified Stock Plan provides for the discretionary award of options, restricted stock and stock purchase rights or any combination of these awards to an eligible person, provided, however, that only NQOs may be granted under the plan. Under the Non-Qualified Stock Plan, the term of any NQO granted may not exceed 10 years, and the exercise price of any such NQO must be at least 85% of the fair market value of the Common Stock at the date of grant. Options generally vest on a monthly basis over a period of four years.

PROPOSAL

At the Annual Meeting, stockholders will be asked to approve amendments to the Company's 2002 Equity Incentive Plan to increase by 400,000 the number of shares of common stock reserved for issuance under the Plan. Such approval will require the affirmative vote of a majority of shares present and voting at the Annual Meeting. The Board of Directors recommends a vote "FOR" the proposal.

PROPOSAL FOUR

RATIFICATION OF INDEPENDENT REGISTERED PUBLIC ACCOUNTANTS

Subject to stockholder ratification, the Audit Committee has selected Odenberg, Ullakko, Muranishi & Co., LLP as independent registered public accountants to audit the financial statements of the Company for the fiscal year ending December 31, 2006.

At the Annual Meeting, the stockholders will be asked to ratify the appointment of Odenberg, Ullakko, Muranishi & Co., LLP as the Company's independent registered public accountants for the fiscal year ending December 31, 2006. Representatives of Odenberg, Ullakko, Muranishi & Co., LLP are expected to be present at the Annual Meeting and will have the opportunity to make statements if they desire to do so. Such representatives are also expected to be available to respond to appropriate questions. A representative from Ernst & Young, LLP will be also available to respond to appropriate questions.

The Board of Directors recommends a vote "FOR" the ratification of the appointment of Odenberg, Ullakko, Muranishi & Co., LLP as the Company's independent registered public accountants for the fiscal year ending December 31, 2006.

FINANCIAL STATEMENTS

The Company's annual report to stockholders for the fiscal year ended December 31, 2005, containing audited balance sheets as of the end of each of the past two fiscal years and audited statements of operations, stockholders' equity and cash flows for each of the last three fiscal years, is being mailed with this Proxy Statement to Stockholders entitled to notice of the Annual Meeting.

STOCKHOLDER PROPOSALS FOR 2007 ANNUAL MEETING

Under the applicable rules of the SEC, a stockholder who wishes to submit a proposal for inclusion in the Proxy Statement of the Board of Directors for the Annual Meeting of Stockholders to be held in the spring of 2007 must submit such proposal in writing to the Secretary of the Company at the Company's principal executive offices no later than December 21, 2006. The applicable rules of the SEC impose certain limitations on the content of proposals and also contain certain eligibility and other requirements (including the requirement that the proponent must have continuously held at least \$2,000 in market value or 1% of the Company's Common Stock for at least one year before the proposal is submitted).

OTHER MATTERS

As of the date of this Proxy Statement, the Board does not intend to bring any other business before the Annual Meeting, and so far as is known to the Board, no other matters will be presented to the Annual Meeting. If, however, any other matter is properly presented at the Annual Meeting, it is intended that proxies in the form enclosed with this Proxy Statement will be voted on such matter in accordance with the judgment of the person or persons voting such proxies, unless the proxy otherwise provides.

BY ORDER OF THE BOARD OF DIRECTORS,

Julian N. Stern, Secretary

Redwood City, California
April 26, 2006

You Are Cordially Invited To Attend The Meeting In Person.

A.P. PHARMA, INC.
 Proxy Solicited by the Board of Directors
 for the Annual Meeting of Stockholders
 to be held May 31, 2006

The undersigned hereby appoints Paul Goddard, Michael O'Connell and Gordon Sangster, or any of them, each with full power of substitution, as the proxyholder(s) of the undersigned to represent the undersigned and vote all the shares of the Common Stock of A.P. Pharma, Inc. (the "Company"), which the undersigned would be entitled to vote if personally present at the Annual Meeting of Stockholders of the Company to be held at the corporate offices at 123 Saginaw Drive, Redwood City, California at 9:00 a.m., local time, on May 31, 2006, and at any adjournments or postponements of such meeting, as stated on the reverse side.

The Board of Directors recommends that you vote FOR the proposals on the reverse side. This proxy, when properly executed, will be voted in the manner directed. WHEN NO CHOICE IS INDICATED THIS PROXY WILL BE VOTED FOR THE FOLLOWING PROPOSALS. This proxy may be revoked by the undersigned at any time, prior to the time it is voted, by any of the means described in the accompanying proxy statement.

CONTINUED AND TO BE SIGNED ON REVERSE SIDE.

Telephone and Internet Voting Instructions

You can vote by telephone OR Internet! Available 24 hours a day 7 days a week!

Instead of mailing your proxy, you may choose one of the two voting methods outlined below to vote your proxy.

To vote using the Telephone
 (within U.S. and Canada)

 Call toll free 1-800-652-VOTE
 (8683) in the United States or
 Canada any time on a touch tone
 telephone. There is NO CHARGE to
 you for the call.

Follow the simple instructions
 provided by the recorded message.

To vote using the Internet

 Go to the following web site:
 WWW.COMPUTERSHARE.COM/EXPRESSVOTE

Enter the information requested
 on your computer screen and
 follow the simple instructions.

VALIDATION DETAILS ARE LOCATED ON THE FRONT OF THIS FORM IN THE COLORED BAR.

If you vote by telephone or the Internet, please DO NOT mail back this proxy card.

Proxies submitted by telephone or the Internet must be received by 1:00 a.m., Central Time, on May 31, 2006.

THANK YOU FOR VOTING

[] Mark this box with an X if you have made changes to your name or address details above.

Annual Meeting Proxy Card
 A Election of Directors

PLEASE REFER TO THE REVERSE SIDE FOR TELEPHONE AND INTERNET VOTING INSTRUCTIONS.

1. To elect as directors, to hold office until the next annual meeting of stockholders and until their successors are elected, the seven nominees listed below.

	For	Withhold
01 - Paul Goddard	[]	[]
02 - Michael O'Connell	[]	[]
03 - Peter Riepenhausen	[]	[]
04 - Toby Rosenblatt	[]	[]
05 - Gregory Turnbull	[]	[]
06 - Dennis Winger	[]	[]
07 - Robert Zerbe	[]	[]

B Issues

The Board of Directors recommends a vote FOR the following proposals.

2. To amend the Company's 1997 Employee Stock Purchase Plan to increase by 150,000 the number of shares of common stock reserved for issuance under the Plan.

FOR	AGAINST	ABSTAIN
[]	[]	[]

3. To amend the Company's 2002 Equity Incentive Plan to increase by 400,000 the number of shares of common stock reserved for issuance under the Plan.

FOR	AGAINST	ABSTAIN
[]	[]	[]

4. To ratify the appointment of Odenberg, Ullakko, Muranishi & Co., LLP as A.P. Pharma's independent registered public accounting firm.

FOR	AGAINST	ABSTAIN
[]	[]	[]

5. In their discretion, the proxyholders are authorized to transact such other business as properly may come before the meeting or any adjournments or postponements of the meeting. The Board of Directors at present knows of no other business to be presented by or on behalf of the Company or the Board of Directors at the meeting.

C Authorized Signatures - Sign Here - This section must be completed for your instructions to be executed.

Date and sign exactly as name(s) appear(s) on this proxy. If signing for estates, trusts, corporations or other entities, title or capacity should be stated. If shares are held jointly, each holder should sign.

Signature 1 -
Please keep signature
within the box

Signature 2 -
Please keep signature
within the box

Date (mm/dd/yyyy)

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2002 Equity Incentive Plan
of
A.P. Pharma, Inc.,
A Delaware corporation

Purpose of this Plan

The purpose of this 2002 Equity Incentive Plan of A.P. Pharma, Inc., a Delaware corporation (the "Company") is to enhance the long-term stockholder value of the Company by offering opportunities to eligible individuals to participate in the growth in value of the equity of the Company.

Definitions and Rules of Interpretation

Definitions. This Plan uses the following defined terms:

"Administrator" means the Board, the Committee, or any officer or employee of the Company to whom the Board or the Committee delegates authority to administer this Plan.

"Affiliate" means a "parent" or "subsidiary" (as each is defined in Section 424 of the Code) of the Company and any other entity that the Board or Committee designates as an "Affiliate" for purposes of this Plan.

"Applicable Law" means any and all laws of whatever jurisdiction, within or without the United States, and the rules of any stock exchange or quotation system on which Shares are listed or quoted, applicable to the taking or refraining from taking of any action under this Plan, including the administration of this Plan and the issuance or transfer of Awards or Award Shares.

"Award" means a Restricted Stock Award or Option granted in accordance with the terms of the Plan.

"Award Agreement" means the document evidencing the grant of an Award.

"Award Shares" means Shares covered by an outstanding Award or purchased under an Award.

"Board" means the board of directors of the Company.

"Change of Control" means any transaction or event that the Board specifies as a Change of Control under Section 10.4.

"Code" means the Internal Revenue Code of 1986.

"Committee" means a committee composed of Company Directors appointed in accordance with the Company's charter documents and Section 4.

"Company Director" means a member of the Board.

"Consultant" means an individual who, or an employee of any entity that, provides bona fide services to the Company or an Affiliate not in connection with the offer or sale of securities in a capital-raising transaction, but who is not an Employee.

"Director" means a member of the board of directors of the Company or an Affiliate.

"Divestiture" means any transaction or event that the Board specifies as a Divestiture under Section 10.5.

"Employee" means a regular employee of the Company or an Affiliate, including an officer or Director who is treated as an employee in the personnel records of the Company or an Affiliate, but not individuals who are classified by the Company or an Affiliate as: (i) leased from or otherwise employed by a third party, (ii) independent contractors, or (iii) intermittent or temporary workers. The Company's or an Affiliate's classification of an individual as an "Employee" (or as not an "Employee") for purposes of this Plan shall not be altered retroactively even if that classification is changed retroactively for another purpose as a result of an audit, litigation or otherwise. A Recipient shall not cease to be an Employee due to transfers between locations of the Company, or between the Company and an Affiliate, or to any successor to the Company or an Affiliate that assumes the Recipient's Options under Section 10. Neither service as a Director nor receipt of a director's fee shall be sufficient to make a Director an "Employee".

"Exchange Act" means the Securities Exchange Act of 1934.

"Executive" means an individual who is subject to Section 16 of the Exchange Act or who is a "covered employee" under Section 162(m) of the Code, in either case because of the individual's relationship with the Company or an Affiliate.

"Expiration Date" means, with respect to an Award, the date stated in the Award Agreement as the expiration date of the Award or, if no such date is stated in the Award Agreement, then the last day of the maximum exercise period for the Award, disregarding the effect of a Recipient's Termination or any other event that would shorten that period.

"Fair Market Value" means the value of Shares as determined under Section 17.2.

"Fundamental Transaction" means any transaction or event described in Section 10.3.

"Grant Date" means the date the Administrator approves the grant of an Award. However, if the Administrator specifies that an Award's Grant Date is a future date or the date on which a condition is satisfied, the Grant Date for such Award is that future date or the date that the condition is satisfied.

"Incentive Stock Option" means an Option intended to qualify as an incentive stock option under Section 422 of the Code and designated as an Incentive Stock Option in the Award Agreement for that Option.

"Listed Security" means any Share listed or approved for listing upon notice of issuance on a national securities exchange or other market system that meets the requirements of Section 25100(o) of the California Securities Law of 1968, as amended.

"Nonstatutory Option" means any Option other than an Incentive Stock Option.

"Objectively Determinable Performance Condition" shall mean a performance condition (i) that is established (x) at the time an Award is granted or (y) no later than the earlier of (1) 90 days after the beginning of the period of service to which it relates, or (2) before the elapse of 25% of the period of service to which it relates, (ii) that is uncertain of achievement at the time it is established, and (iii) the achievement of which is determinable by a third party with knowledge of the relevant facts. Examples of measures that may be used in Objectively Determinable Performance Conditions include net order dollars, net profit dollars, net profit growth, net revenue dollars, revenue growth, individual performance, earnings per share, return on assets, return on equity, and other financial objectives, objective customer satisfaction indicators and efficiency measures, each with respect to the Company and/or an individual business unit.

"Officer" means an officer of the Company as defined in Rule 16a-1 adopted under the Exchange Act.

"Option" means a right to purchase Shares of the Company granted under this Plan.

"Option Price" means the price payable under an Option for Shares, not including any amount payable in respect of withholding or other taxes.

"Option Shares" means Shares covered by an outstanding Option or purchased under an Option.

"Plan" means this 2002 Equity Incentive Plan of A.P. Pharma, Inc.

"Purchase Price" means the price payable under a Restricted Stock Award for Shares, not including any amount payable in respect of withholding or other taxes.

"Qualified Domestic Relations Order" means a judgment, order, or decree meeting the requirements of Section 414(p) of the Code.

"Recipient" means: (i) a person to whom an Award has been granted, including a holder of a Substitute Award, (ii) a person to whom an Award has been transferred in accordance with all applicable requirements of Sections 6.5, 7(h) and 16, and (iii) a person who holds Option Shares subject to any right of repurchase under Section 15.2.

"Restricted Stock Award" means an offer by the Company to sell shares subject to certain restrictions pursuant to the Award Agreement as

described in Section 8.

"Reverse Vesting" means, with respect to an Option, that an Option is or was fully exercisable but that, subject to a "reverse" vesting schedule, the Company has a right to repurchase the Option Shares as specified in Section 15.2(a), with the Company's right of repurchase expiring in accordance with the "forward" vesting schedule that would otherwise have applied to the Option under which the Option Shares were purchased or other vesting schedule described in the Award Agreement. With respect to a Restricted Stock Award, Reverse Vesting means that the Company has a right to repurchase the Award Shares purchased pursuant to the Restricted Stock Award, as specified in Section 15.2(a), with the Company's right of repurchase expiring in accordance with the vesting schedule in the Award Agreement.

"Rule 16b-3" means Rule 16b-3 adopted under Section 16(b) of the Exchange Act.

"Securities Act" means the Securities Act of 1933.

"Share" means a share of the common stock of the Company or other securities substituted for the common stock under Section 10.

"Substitute Option" means an Option granted in substitution for, or upon the conversion of, an option granted by another entity to purchase equity securities in the granting entity.

"Substitute Restricted Stock Award" means a Restricted Stock Award granted in substitution for, or upon the conversion of, a stock award granted by another entity to purchase equity securities in the granting entity.

"Ten Percent Stockholder" means any person who, directly or by attribution under Section 424(d) of the Code, owns stock possessing more than ten percent of the total combined voting power of all classes of stock of the Company or of any Affiliate on the Grant Date.

"Termination" means that the Recipient has ceased to be, with or without any cause or reason, an Employee, Director or Consultant. However, unless so determined by the Administrator, "Termination" shall not include a change in status from an Employee, Consultant or Director to another such status. An event that causes an Affiliate to cease being an Affiliate shall be treated as the "Termination" of that Affiliate's Employees, Directors, and Consultants.

Rules of Interpretation. Any reference to a "Section", without more, is to a Section of this Plan. Captions and titles are used for convenience in this Plan and shall not, by themselves, determine the meaning of this Plan. Except when otherwise indicated by the context, the singular includes the plural and vice versa. Any reference to a statute is also a reference to the applicable rules and regulations adopted under that statute. Any reference to a statute, rule or regulation, or to a section of a statute, rule or regulation, is a reference to that statute, rule, regulation, or section as amended from time to time, both before and after the effective date of this Plan and including any successor provisions.

Shares Subject to this Plan; Term of this Plan

Number of Award Shares. Subject to adjustment under Section 10, the maximum number of Shares that may be issued under this Plan is 1,700,000.

Source of Shares. Award Shares may be authorized but unissued Shares or treasury Shares. If an Award is terminated, expires, or otherwise becomes unexercisable without having been exercised in full, the unpurchased Shares that were subject to the Award shall revert to this Plan and shall again be available for future issuance under this Plan. Shares actually issued under this Plan shall not be available for regrant even if repurchased by the Company.

Term of this Plan

This Plan shall be effective on the date it is approved by the Board. However, no Award may be exercised unless and until the Company's stockholders approve this Plan within 12 months after the Board approves this Plan.

Subject to Section 13, this Plan shall continue in effect for a period of ten years from the earlier of the date on which the Plan was adopted by the Board and the date on which the Plan was approved by the Company's stockholders.

General

The Board shall have ultimate responsibility for administering this Plan. The Board may delegate certain of its responsibilities to a Committee, which shall consist of at least two members of the Board. The Board or the Committee may further delegate its responsibilities to any Employee of the Company or any Affiliate. Where this Plan specifies that an action is to be taken or a determination made by the Board, only the Board may take that action or make that determination. Where this Plan specifies that an action is to be taken or a determination made by the Committee, only the Committee may take that action or make that determination. Where this Plan references the "Administrator", the action may be taken or determination made by the Board, the Committee, or other Administrator. However, only the Board or the Committee may approve grants of Awards to Executives, and an Administrator other than the Board or the Committee may grant Awards only within guidelines established by the Board or Committee. Moreover, all actions and determinations by any Administrator are subject to the provisions of this Plan.

So long as the Company has registered and outstanding a class of equity securities under Section 12 of the Exchange Act, the Committee shall consist of Company Directors who are "Non-Employee Directors" as defined in Rule 16b-3 and, after the expiration of any transition period permitted by Treasury Regulations Section 1.162-27(h)(3), who are "outside directors" as defined in Section 162(m) of the Code.

Authority of Administrator. Subject to the other provisions of this Plan, the Administrator shall have the authority:

- to grant Awards, including Substitute Awards;
- to determine the Fair Market Value of Shares;
- to determine the Option Price and the Purchase Price under Awards;
- to select the Recipients;
- to determine the times Awards are granted;
- to determine the number of Shares subject to each Award;
- to determine the types of payment that may be used to purchase Award Shares;
- to determine the types of payment that may be used to satisfy withholding tax obligations;
- to determine the other terms of each Award, including but not limited to the time or times at which Awards may be exercised, whether and under what conditions an Award is assignable, and whether an Option is a Nonstatutory Option or an Incentive Stock Option;
- to modify or amend any Award;
- to authorize any person to sign any Award Agreement or other document related to this Plan on behalf of the Company;
- to determine the form of any Award Agreement or other document related to this Plan, and whether that document, including signatures, may be in electronic form;
- to interpret this Plan and any Award Agreement or document related to this Plan;
- to correct any defect, remedy any omission, or reconcile any inconsistency in this Plan, any Award Agreement or any other document related to this Plan;
- to adopt, amend, and revoke rules and regulations under this Plan, including rules and regulations relating to sub-plans and Plan addenda;
- to adopt, amend, and revoke rules and procedures relating to the operation and administration of this Plan to accommodate non-U.S. Recipients and the requirements of Applicable Law such as: (i) rules and procedures regarding the conversion of local currency, withholding procedures and the handling of stock certificates to comply with local practice and requirements, and (ii) sub-plans and Plan addenda for non-U.S.

Recipients; and

to make all other determinations the Administrator deems necessary or advisable for the administration of this Plan.

Scope of Discretion. Subject to the specific provisions and specific limitations of this Plan, as well as all rights conferred on specific Recipients by Award Agreements and other agreements, (i) on all matters for which this Plan confers the authority, right or power on the Board, the Committee, or other Administrator to make decisions, that body may make those decisions in its sole and absolute discretion and (ii) in making those decisions, the Board, Committee or other Administrator need not treat all persons eligible to receive Awards, all Recipients, all Awards or all Award Shares the same way.

Persons Eligible to Receive Awards

Eligible Individuals. Awards (including Substitute Awards) may be granted to, and only to, Employees, Directors and Consultants, including prospective Employees, Directors and Consultants conditioned on the beginning of their service for the Company or an Affiliate.

Section 162(m) Limitation.

Options. So long as the Company is a "publicly held corporation" within the meaning of Section 162(m) of the Code: (a) no Employee or prospective Employee may be granted one or more Options within any fiscal year of the Company to purchase more than 250,000 Shares under Options, subject to adjustment under Section 10, and (b) Options may be granted to an Executive only by the Committee (and, notwithstanding Section 4.1(a), not by the Board). If an Option is cancelled without being exercised or if the Option Price of an Option is reduced, that cancelled or repriced Option shall continue to be counted against the limit on Shares under this Section 5.2.

Restricted Stock Awards. Any Restricted Stock Award intended as "qualified performance-based compensation" within the meaning of Section 162(m) of the Code must vest or become exercisable contingent on the achievement of one or more Objectively Determinable Performance Conditions, the Restricted Stock Award may be granted only by the Committee, and the material terms of the Award, including the maximum amount of the Award and the Award formula, must be approved by the stockholders of the Company before the Award Shares under such Restricted Stock Award are issued.

Terms and Conditions of Options

The following rules apply to all Options:

Price. No Option intended as "qualified incentive-based compensation" within the meaning of Section 162(m) of the Code may have an Option Price less than 100% of the Fair Market Value of the Shares on the Grant Date. In no event will the Option Price of any Option be less than the par value of the Shares issuable under the Option if that is required by Applicable Law.

Term. No Option shall be exercisable after its Expiration Date. No Option may have an Expiration Date that is more than ten years after its Grant Date.

Vesting. Options shall be exercisable: (a) on the Grant Date, or (b) in accordance with a schedule related to the Grant Date, the date the Recipient's directorship, employment or consultancy begins, or a different date specified in the Option Agreement. If so provided in the Option Agreement, an Option may be exercisable subject to the application of Reverse Vesting to the Option Shares.

Form of Payment.

The Administrator shall determine the acceptable form and method of payment for exercising an Option.

Acceptable forms of payment for all Option Shares are cash, check or wire transfer, denominated in U.S. dollars except as specified by the Administrator for non-U.S. Employees or non-U.S. sub-plans.

In addition, the Administrator may permit payment to be made by any of the following methods:

other Shares, or the designation of other Shares, which (A) in the case of Shares acquired upon exercise of an option (whether or not under

this Plan) have been owned by the Recipient for more than six months on the date of surrender, and (B) have a Fair Market Value on the date of surrender equal to the Option Price of the Shares as to which the Option is being exercised;

provided that a public market exists for the Shares, through a "same day sale" commitment from the Recipient and a broker-dealer that is a member of the National Association of Securities Dealers (an "NASD Dealer") under which the Recipient irrevocably instructs the NASD Dealer promptly to forward an amount equal to the Option Price directly to the Company (a "Cashless Exercise").

one or more full recourse promissory notes bearing interest at a fair market value rate that is at least sufficient to avoid imputation of interest under Sections 483, 1274 and 7872 of the Code and with such other terms as the Administrator specifies, except that Consultants may not purchase Shares with a promissory note unless the note is adequately secured by collateral other than the Shares, the portion of the Option Price equal to the par value of the Shares must be paid in cash or other lawful consideration, other than the note, if that is required by Applicable Law, and the Company shall at all times comply with any applicable margin rules of the Federal Reserve; and

any combination of the methods of payment permitted by any paragraph of this Section 6.4.

Nonassignability of Options. Except as set forth in any Option Agreement, no Option shall be assignable or otherwise transferable by the Recipient except by will or by the laws of descent and distribution. However, Options may be transferred and exercised in accordance with a Qualified Domestic Relations Order.

Substitute Options. The Board may cause the Company to grant Substitute Options in connection with the acquisition by the Company or an Affiliate of equity securities of any entity (including by merger) or all or a portion of the assets of any entity. Any such substitution shall be effective when the acquisition closes. Substitute Options may be Nonstatutory Options or Incentive Stock Options. Unless and to the extent specified otherwise by the Board, Substitute Options shall have the same terms and conditions as the options they replace, except that (subject to Section 10) Substitute Options shall be Options to purchase Shares rather than equity securities of the granting entity and shall have an Option Price that, as determined by the Board in its sole and absolute discretion, properly reflects the substitution.

Incentive Stock Options

The following rules apply only to Incentive Stock Options and only to the extent these rules are more restrictive than the rules that would otherwise apply under this Plan. With the consent of the Recipient, or where this Plan provides that an action may be taken notwithstanding any other provision of this Plan, the Administrator may deviate from the requirements of this Section, notwithstanding that any Incentive Stock Option modified by the Administrator will thereafter be treated as a Nonstatutory Option.

The Expiration Date of an Incentive Stock Option shall not be later than ten years from its Grant Date, with the result that no Incentive Stock Option may be exercised after the expiration of ten years from its Grant Date.

No Incentive Stock Option may be granted more than ten years from the date this Plan was approved by the Board.

Options intended to be incentive stock options under Section 422 of the Code that are granted to any single Recipient under all incentive stock option plans of the Company and its Affiliates, including incentive stock options granted under this Plan, may not vest at a rate of more than \$100,000 in Fair Market Value of stock (measured on the grant dates of the options) during any calendar year. For this purpose, an option vests with respect to a given share of stock the first time its holder may purchase that share, notwithstanding any right of the Company to repurchase that share. Unless the Administrator specifies otherwise in the related agreement governing the option, this vesting limitation shall be applied by, to the extent necessary to satisfy this \$100,000 rule, treating certain stock options that were intended to be incentive stock options under Section 422 of the Code as Nonstatutory Options. The stock options or portions of stock options to be reclassified as Nonstatutory Options are those with the highest option prices, whether granted under this Plan or any other equity compensation plan of the Company or any Affiliate that permits that treatment. This Section 7(c) shall not cause an Incentive Stock Option to vest before its original vesting date or cause an Incentive

Stock Option that has already vested to cease to be vested.

In order for an Incentive Stock Option to be exercised for any form of payment other than those described in Section 6.4(b), that right must be stated in the Option Agreement relating to that Incentive Stock Option. Any Incentive Stock Option granted to a Ten Percent Stockholder, must have an Expiration Date that is not later than five years from its Grant Date, with the result that no such Option may be exercised after the expiration of five years from the Grant Date.

The Option Price of an Incentive Stock Option shall never be less than the Fair Market Value of the Shares at the Grant Date. The Option Price for the Shares covered by an Incentive Stock Option granted to a Ten Percent Stockholder shall never be less than 110% of the Fair Market Value of the Shares at the Grant Date.

Incentive Stock Options may be granted only to Employees. If a Recipient changes status from an Employee to a Consultant, that Recipient's Incentive Stock Options become Nonstatutory Options if not exercised within the time period described in Section 7(i).

No rights under an Incentive Stock Option may be transferred by the Recipient, other than by will or the laws of descent and distribution. During the life of the Recipient, an Incentive Stock Option may be exercised only by the Recipient. The Company's compliance with a Qualified Domestic Relations Order, or the exercise of an Incentive Stock Option by a guardian or conservator appointed to act for the Recipient, shall not violate this Section 7(h).

An Incentive Stock Option shall be treated as a Nonstatutory Option if it remains exercisable after, but is not exercised within, the three-month period beginning with the Recipient's Termination for any reason other than the Recipient's death or disability (as defined in Section 22(c) of the Code). In the case of Termination due to death or disability, an Incentive Stock Option shall be treated as a Nonstatutory Option if it remains exercisable after, but is not exercised within, one year after the Recipient's Termination.

Restricted Stock Awards

The following rules apply to all Restricted Stock Awards:

Price; Payment. The Purchase Price for the Award Shares issuable under a Restricted Stock Award shall be determined by the Administrator; provided that in no event shall such Purchase Price be less than the par value of the Award Shares issuable under the Restricted Stock Award.

Term. No Restricted Stock Award shall be exercisable after its Expiration Date. No Restricted Stock Award may have an Expiration Date that is more than ten years after its Grant Date.

Vesting. Restricted Stock Awards shall be exercisable: (a) on the Grant Date, or (b) in accordance with a schedule related to the Grant Date, the date the Recipient's directorship, employment or consultancy begins, or a different date specified in the Award Agreement.

Restriction Period. Subject to this Plan and the Award Agreement, during a period set by the Administrator, commencing with the Grant Date of the Restricted Stock Award and ending not less than three (3) years and not more than ten (10) years from such Grant Date, the Recipient shall not be permitted to sell, assign, transfer, pledge or otherwise encumber the Award Shares of a Restricted Stock Award. Within these limits, the Administrator may provide for the lapse of such restrictions in installments, but, subject to Sections 10.3 and 10.4, may not accelerate or waive such restrictions.

Right of Repurchase. If so provided in the Award Agreement, Award Shares acquired pursuant to a Restricted Stock Award may be subject to Reverse Vesting.

Form of Payment. The Administrator shall determine the acceptable form and method of payment for exercising a Restricted Stock Award.

Acceptable forms of payment for all Award Shares are cash, check or wire transfer, denominated in U.S. dollars except as specified by the Administrator for non-U.S. Employees or non-U.S. sub-plans.

In addition, the Administrator may permit payment to be made by any of the methods permitted with respect to the exercise of Options pursuant to Section 6.4.

Nonassignability of Restricted Stock Awards. Except as set forth in

any Award Agreement, no Restricted Stock Award shall be assignable or otherwise transferable by the Recipient except by will or by the laws of descent and distribution. However, Restricted Stock Awards may be transferred and exercised in accordance with a Qualified Domestic Relations Order.

Substitute Restricted Stock Award. The Board may cause the Company to grant Substitute Restricted Stock Awards in connection with the acquisition by the Company or an Affiliate of equity securities of any entity (including by merger) or all or a portion of the assets of any entity. Unless and to the extent specified otherwise by the Board, Substitute Restricted Stock Awards shall have the same terms and conditions as the options they replace, except that (subject to Section 10) Substitute Restricted Stock Awards shall be Restricted Stock Awards to purchase Shares rather than equity securities of the granting entity and shall have a Purchase Price that, as determined by the Board in its sole and absolute discretion, properly reflects the substitution.

Exercise of Awards

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In General. An Award shall be exercisable in accordance with this Plan, the Award Agreement under which it is granted, and as prescribed by the Administrator.

Time of Exercise. Options and Restricted Stock Awards shall be considered exercised when the Company receives: (a) written notice of exercise from the person entitled to exercise the Option or Restricted Stock Award, (b) full payment, or provision for payment, in a form and method approved by the Administrator, for the Shares for which the Option or Restricted Stock Award is being exercised, and (c) with respect to Nonstatutory Options, payment, or provision for payment, in a form approved by the Administrator, of all applicable withholding taxes due upon exercise. An Award may not be exercised for a fraction of a Share.

Issuance of Award Shares. The Company shall issue Award Shares in the name of the person properly exercising the Award. If the Recipient is that person and so requests, the Award Shares shall be issued in the name of the Recipient and the Recipient's spouse. The Company shall endeavor to issue Award Shares promptly after an Award is exercised. However, until Award Shares are actually issued, as evidenced by the appropriate entry on the stock books of the Company or its transfer agent, no right to vote or receive dividends or other distributions, and no other rights as a stockholder, shall exist with respect to the Award Shares, even though the Recipient has completed all the steps necessary to exercise the Award. No adjustment shall be made for any dividend, distribution, or other right for which the record date precedes the date the Award Shares are issued, except as provided in Section 10.

Termination

In General. Except as provided by the Administrator, including in an Award Agreement, and as otherwise provided in Sections 9.4(b), (c), (d), (e), (f) and (g), after a Recipient's Termination, the Recipient's Awards shall be exercisable to the extent (but only to the extent) they are vested on the date of that Termination and only during the period ending three months after the Termination, but in no event after the Expiration Date. To the extent the Recipient does not exercise an Award within the time specified for exercise, the Award shall automatically terminate. With respect to Restricted Stock Awards, except to the extent otherwise provided by the Administrator, including in the Award Agreement and in accordance with Section 10, upon termination of a Recipient's employment for any reason during the restriction period provided for in Section 8(d), all Award Shares of a Restricted Stock Award still subject to such restriction period shall be forfeited by the Recipient and to the extent previously purchased by the Recipient shall be repurchased by the Company for an amount equal to the original Purchase Price.

Leaves of Absence. Unless otherwise provided in the Award Agreement, no Award may be exercised more than three months after the beginning of a leave of absence, other than a personal or medical leave approved by the Administrator with employment guaranteed upon return. Awards shall not continue to vest during a leave of absence, other than an approved personal or medical leave with employment guaranteed upon return.

Death or Disability. Unless otherwise provided in the Award Agreement, if a Recipient's Termination is due to death or disability (as determined by the Administrator with respect to all Awards other than Incentive Stock Options and as defined by Section 22(e) of the Code with respect to Incentive Stock Options), all Awards of that Recipient to the extent exercisable at the date of that Termination may be exercised for one year after that Termination, but in no event after the Expiration Date. In the

case of Termination due to death, an Award may be exercised as provided in Section 16. In the case of Termination due to disability, if a guardian or conservator has been appointed to act for the Recipient and been granted this authority as part of that appointment, that guardian or conservator may exercise the Award on behalf of the Recipient. In the case of a Recipient who dies or become disabled within three months after Termination, if the Termination was not due to Cause, the Recipient's Awards may be exercised for one year after that Termination. To the extent an Award is not so exercised within the time specified for its exercise, the Award shall automatically terminate.

Divestiture. If a Recipient's Termination is due to a Divestiture, the Board may take any one or more of the actions described in Section 10.3 or 10.4.

Retirement. Unless otherwise provided in the Award Agreement by the Administrator, if a Recipient's Termination is due to the Recipient's retirement in accordance with the Company's or an Affiliate's retirement policy, all Awards of that Recipient to the extent exercisable at the Recipient's date of retirement may be exercised for one year after the Recipient's date of retirement, but in no event after the Expiration Date. To the extent the Recipient does not exercise an Option within the time specified for exercise, the Award shall automatically terminate.

Severance Programs. Unless otherwise provided in the Award Agreement by the Administrator, if a Recipient's Termination results from participation in a voluntary severance incentive program of the Company or an Affiliate approved by the Board, all Awards of that Employee to the extent exercisable at the time of that Termination shall be exercisable for one year after the Recipient's Termination, but in no event after the Expiration Date. If the Recipient does not exercise an Award within the time specified for exercise, the Award shall automatically terminate.

Termination for Cause. If a Recipient's Termination is due to cause, all of the Recipient's Awards shall automatically terminate and cease to be exercisable at the time of Termination and all Awards exercised after the first event constituting cause may be rescinded by the Administrator. "Cause" means dishonesty, fraud, misconduct, disclosure or misuse of confidential information, conviction of, or a plea of guilty or no contest to, a felony or similar offense, habitual absence from work for reasons other than illness, or intentional conduct that could cause significant injury to the Company or an Affiliate, in each case as determined by the Administrator.

Reverse Vesting. Under any circumstances stated in this Section 9.4 in which all unvested Options of a Recipient immediately vest, the Company's repurchase rights shall lapse on all Option Shares held by that Recipient that are subject to Reverse Vesting.

Consulting or Employment Relationship. Nothing in this Plan or in any Award Agreement, and no Award or the fact that Award Shares remain subject to repurchase rights, shall: (a) interfere with or limit the right of the Company or any Affiliate to terminate the employment or consultancy of any Recipient at any time, whether with or without cause or reason, and with or without the payment of severance or any other compensation or payment, or (b) interfere with the application of any provision in any of the Company's or any Affiliate's charter documents or Applicable Law relating to the election, appointment, term of office, or removal of a Director.

Certain Transactions and Events
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In General. Except as specifically provided in this Section 10, no change in the capital structure of the Company, merger, sale or other disposition of assets or a subsidiary, change of control, issuance by the Company of shares of any class of securities convertible into shares of any class, conversion of securities, or other transaction or event shall require or be the occasion for any adjustments of the type described in this Section 10.

Changes in Capital Structure. In the event of any stock split, reverse stock split, recapitalization, combination or reclassification of stock, stock dividend, spin-off, or similar change to the capital structure of the Company (not including a Fundamental Transaction or Change of Control), the Board shall make whatever adjustments it concludes are appropriate to: (a) the number and type of Awards that may be granted under this Plan, (b) the number and type of Options that may be granted to any individual under this Plan, (c) the Purchase Price of any Restricted Stock Award, (d) the Option Price and number and class of securities issuable under each outstanding Option, and (e) the repurchase price of any securities substituted for Option Shares that are subject to repurchase rights. The specific adjustments shall be determined by the Board in its sole and absolute

discretion. Unless the Board specifies otherwise, any securities issuable as a result of any such adjustment shall be rounded to the next lower whole security.

Fundamental Transactions. If the Company merges with another entity in a transaction in which the Company is not the surviving entity or if, as a result of any other transaction or event, other securities are substituted for the Shares or Shares may no longer be issued (each a "Fundamental Transaction"), then, notwithstanding any other provision of this Plan, the Board shall do one or more of the following contingent on the closing or completion of the Fundamental Transaction: (a) arrange for the substitution of options or other compensatory awards on equity securities other than Shares (including, if appropriate, equity securities of an entity other than the Company) in exchange for Awards, (b) accelerate the vesting and termination of outstanding Awards, in whole or in part, so that Awards can be exercised before or otherwise in connection with the closing or completion of the transaction or event but then terminate, (c) cancel Awards in exchange for cash payments to Recipients, (d) either arrange for any repurchase rights of the Company with respect to Award Shares to apply to the securities issued in substitution for Shares or terminate repurchase rights on Award Shares. The Board need not adopt the same rules for each Award or each Recipient.

Changes of Control. The Board may also, but need not, specify that other transactions or events constitute a "Change of Control". The Board may do that either before or after the transaction or event occurs. Examples of transactions or events that the Board may treat as Changes of Control are: (a) the Company or an Affiliate is a party to a merger, consolidation, amalgamation, or other transaction in which the beneficial stockholders of the Company, immediately before the transaction, beneficially own securities representing 50% or less of the total combined voting power or value of the Company immediately after the transaction, (b) any person or entity, including a "group" as contemplated by Section 13(d)(3) of the Exchange Act, acquires securities holding 30% or more of the total combined voting power or value of the Company, or (c) as a result of or in connection with a contested election of Company Directors, the persons who were Company Directors immediately before the election cease to constitute a majority of the Board. In connection with a Change of Control, notwithstanding any other provision of this Plan, the Board may take any one or more of the actions described in Section 10.3. In addition, the Board may extend the date for the exercise of Awards (but not beyond their original Expiration Date). The Board need not adopt the same rules for each Award or each Recipient.

Divestiture. If the Company or an Affiliate sells or otherwise transfers equity securities of an Affiliate to a person or entity other than the Company or an Affiliate, or leases, exchanges or transfers all or any portion of its assets to such a person or entity, then the Board, in its sole and absolute discretion, may specify that such transaction or event constitutes a "Divestiture". In connection with a Divestiture, notwithstanding any other provision of this Plan, the Board may take one or more of the actions described in Section 10.3 or 10.4 with respect to Awards or Award Shares held by, for example, Employees, Directors or Consultants for whom that transaction or event results in a Termination. The Board need not adopt the same rules for each Award or each Recipient.

Dissolution. If the Company adopts a plan of dissolution, the Board may, in its sole and absolute discretion, cause Awards to be fully vested and exercisable (but not after their Expiration Date) before the dissolution is completed but contingent on its completion and may cause the Company's repurchase rights on Award Shares to lapse upon completion of the dissolution. To the extent not exercised before the earlier of the completion of the dissolution or their Expiration Date, Awards shall terminate just before the dissolution is completed. The Board need not adopt the same rules for each Award or each Recipient.

Cut-Back to Preserve Benefits. If the Administrator determines that the net after-tax amount to be realized by any Recipient, taking into account any accelerated vesting, termination of repurchase rights, or cash payments to that Recipient in connection with any transaction or event addressed in this Section 10 would be greater if one or more of those steps were not taken with respect to that Recipient's Awards or Award Shares, then and to the extent determined by the Administrator, one or more of those steps shall not be taken.

Withholding and Tax Reporting -----

Tax Withholding Alternatives

General. Whenever Award Shares are issued or become free of restrictions, the Company may require the Recipient to remit to the Company

an amount sufficient to satisfy any applicable tax withholding requirement, whether the related tax is imposed on the Recipient or the Company. The Company shall have no obligation to deliver Award Shares or release Award Shares from an escrow until the Recipient has satisfied those tax withholding obligations. Whenever payment in satisfaction of Awards is made in cash, the payment will be reduced by an amount sufficient to satisfy all tax withholding requirements.

Method of Payment. The Recipient shall pay any required withholding using the forms of consideration described in Section 6.4(b), except that, in the discretion of the Administrator, the Company may also permit the Recipient to use any of the forms of payment described in Section 6.4(c). The Administrator may also permit Award Shares to be withheld to pay required withholding. If the Administrator permits Award Shares to be withheld, the Fair Market Value of the Award Shares withheld shall not exceed the amount determined by the applicable minimum statutory withholding rates, and shall be determined as of the date that the amount of tax to be withheld or tendered for this purpose is to be determined.

Reporting of Dispositions. Any holder of Option Shares acquired under an Incentive Stock Option shall promptly notify the Administrator in writing of the sale or other disposition of any of those Option Shares if the disposition occurs during: (a) the longer of two years after the Grant Date of the Incentive Stock Option and one year after the date the Incentive Stock Option was exercised, or (b) such other period as the Administrator has established.

Compliance with Law

Applicable Law. The grant of Awards and the issuance and subsequent transfer of Award Shares shall be subject to compliance with all Applicable Law, including all applicable securities laws. Awards may not be exercised, and Award Shares may not be transferred, in violation of Applicable Law. Thus, for example, Awards may not be exercised unless: (a) a registration statement under the Securities Act is then in effect with respect to the related Award Shares, or (b) in the opinion of legal counsel to the Company, those Award Shares may be issued in accordance with an applicable exemption from the registration requirements of the Securities Act and any other applicable securities laws. The failure or inability of the Company to obtain from any regulatory body the authority considered by the Company's legal counsel to be necessary or useful for the lawful issuance of any Award Shares or their subsequent transfer shall relieve the Company of any liability for failing to issue those Award Shares or permitting their transfer. As a condition to the exercise of any Award or the transfer of any Award Shares, the Company may require the Recipient to satisfy any requirements or qualifications that may be necessary or appropriate to comply with or evidence compliance with any Applicable Law.

Amendment or Termination of this Plan or Outstanding Awards

Amendment and Termination. The Board may at any time amend, suspend, or terminate this Plan.

Stockholder Approval. The Company shall obtain the approval of the Company's stockholders for any amendment to this Plan if stockholder approval is necessary or desirable to comply with any Applicable Law or with the requirements applicable to the grant of Awards intended to be Incentive Stock Options. The Board may also, but need not, require that the Company's stockholders approve any other amendments to this Plan.

Effect. No amendment, suspension, or termination of this Plan, and no modification of any Award even in the absence of an amendment, suspension, or termination of this Plan, shall impair any existing contractual rights of any Recipient unless the affected Recipient consents to the amendment, suspension, termination, or modification. However, no such consent shall be required if the Administrator determines, in its sole and absolute discretion, that the amendment, suspension, termination, or modification: (a) is required or advisable in order for the Company, the Plan or the Award to satisfy Applicable Law or to meet the requirements of any accounting standard; or (b) in connection with any transaction or event described in Section 10, is in the best interests of the Company or its stockholders. The Administrator may, but need not, take the tax consequences to affected Recipients into consideration in acting under the preceding sentence. Termination of this Plan shall not affect the Administrator's ability to exercise the powers granted to it under this Plan with respect to Awards granted before the termination, or Award Shares issued under such Awards, even if those Award Shares are issued after the termination.

Reserved Rights
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Nonexclusivity of this Plan. This Plan shall not limit the power of the Company or any Affiliate to adopt other incentive arrangements including, for example, the grant or issuance of stock options, stock, or other equity-based rights under other plans or independently of any plan.

Unfunded Plan. This Plan shall be unfunded. Although bookkeeping accounts may be established with respect to Recipients, any such accounts will be used merely as a convenience. The Company shall not be required to segregate any assets on account of this Plan, the grant of Awards, or the issuance of Award Shares. The Company and the Administrator shall not be deemed to be a trustee of stock or cash to be awarded under this Plan. Any obligations of the Company to any Recipient shall be based solely upon contracts entered into under this Plan, such as Award Agreements. No such obligation shall be deemed to be secured by any pledge or other encumbrance on any assets of the Company. Neither the Company nor the Administrator shall be required to give any security or bond for the performance of any such obligation.

Special Arrangements Regarding Award Shares
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Escrows and Pledges. To enforce any restrictions on Award Shares including restrictions related to Reverse Vesting, the Administrator may require their holder to deposit the certificates representing Award Shares, with stock powers or other transfer instruments approved by the Administrator endorsed in blank, with the Company or an agent of the Company to hold in escrow until the restrictions have lapsed or terminated. The Administrator may also cause a legend or legends referencing the restrictions to be placed on the certificates. Any Recipient who delivers a promissory note as partial or full consideration for the purchase of Award Shares will be required to pledge and deposit, with the Company, some or all of the Award Shares as collateral to secure the payment of the note. However, the Administrator may require or accept other or additional forms of collateral to secure the note and, in any event, the Company will have full recourse against the maker of the note, notwithstanding any pledge or other collateral, unless stated otherwise in the Award Agreement and the note.

Repurchase Rights

Reverse Vesting. If an Option or Restricted Stock Award is subject to Reverse Vesting, the Company shall have the right, during the seven months after the Recipient's Termination, to repurchase any or all of the Award Shares that were unvested as of the date of that Termination, for a price equal to the lower of: (i) the Option Price or Purchase Price for such Shares, minus the amount of any cash dividends paid or payable with respect to the Award Shares for which the record date precedes the repurchase, and (ii) the Fair Market Value of those Option Shares as of the date of the Termination. The repurchase price shall be paid in cash or, if the Option Shares were purchased in whole or in part for a promissory note, cancellation of indebtedness under that note, or a combination of those means. The Company may assign this right of repurchase.

Procedure. The Company or its assignee may choose to give the Recipient a written notice of exercise of its repurchase rights under this Section 15.2. However, the Company's failure to give such a notice shall not affect its rights to repurchase Award Shares. The Company must, however, tender the repurchase price during the period specified in this Section 15.2 for exercising its repurchase rights in order to exercise such rights.

Market Standoff. If requested by the Company or a representative of its underwriters in connection with a public offering of any securities of the Company registered under the Securities Act, Recipients or certain Recipients shall be prohibited from selling some or all of their Award Shares during a period not to exceed 180 days after the effective date of any registration statement of the Company.

Dividends. Dividends on Award Shares that are subject to any restrictions, including Reverse Vesting, shall be subject to the same restriction, including those set forth in this Section 15, as the Award Shares on which the dividends were paid.

Beneficiaries
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A Recipient may file a written designation of one or more beneficiaries who are to receive the Recipient's rights under the Recipient's Awards after the Recipient's death. A Recipient may change such a designation at

any time by written notice. If a Recipient designates a beneficiary, the beneficiary may exercise the Recipient's Awards after the Recipient's death. If a Recipient dies when the Recipient has no living beneficiary designated under this Plan, the Company shall allow the executor or administrator of the Recipient's estate to exercise the Award or, if there is none, the person entitled to exercise the Option under the Recipient's will or the laws of descent and distribution. In any case, no Award may be exercised after its Expiration Date.

Miscellaneous
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Governing Law. This Plan and all determinations made and actions taken under this Plan shall be governed by the substantive laws, but not the choice of law rules, of the State of Delaware.

Determination of Value. Fair Market Value shall be determined as follows:

Listed Stock. If the Shares are traded on any established stock exchange or quoted on a national market system, Fair Market Value shall be the closing sales price for the Shares as quoted on that stock exchange or system for the date the value is to be determined (the "Value Date") as reported in The Wall Street Journal or a similar publication. If no sales are reported as having occurred on the Value Date, Fair Market Value shall be that closing sales price for the last preceding trading day on which sales of Shares are reported as having occurred. If no sales are reported as having occurred during the five trading days before the Value Date, Fair Market Value shall be the closing bid for Shares on the Value Date. If Shares are listed on multiple exchanges or systems, Fair Market Value shall be based on sales or bids on the primary exchange or system on which Shares are traded or quoted.

Reservation of Shares. During the term of this Plan, the Company will at all times reserve and keep available such number of Shares as are still issuable under this Plan.

Electronic Communications. Any Award Agreement, notice of exercise of an Award, or other document required or permitted by this Plan may be delivered in writing or, to the extent determined by the Administrator, electronically. Signatures may also be electronic if permitted by the Administrator.

Notices. Unless the Administrator specifies otherwise, any notice to the Company under any Option Agreement or with respect to any Awards or Award Shares shall be in writing (or, if so authorized by Section 17.4, communicated electronically), shall be addressed to the Secretary of the Company, and shall only be effective when received by the Secretary of the Company.

Adopted by the Board on: April 4, 2002

Approved by the stockholders on: May 22, 2002

Effective date of this Plan: April 4, 2002

Amended by the Board on: March 25, 2004

Approved by the stockholders on: May 25, 2004

Effective date of this Plan: March 25, 2004

Amended by the Board on: January 11, 2005

Approved by the stockholders on: May 25, 2005

Effective date of this Plan: January 11, 2005

Amended by the Board on: January 10, 2006

Approved by the stockholders on:

Effective date of this Plan: -----

(Footnote continued)

ADVANCED POLYMER SYSTEMS, INC.

1997 EMPLOYEE STOCK PURCHASE PLAN

1. PURPOSE. This Advanced Polymer Systems, Inc. 1997 Employee Stock Purchase Plan is designed to encourage and assist employees of Advanced Polymer Systems, Inc. and participating subsidiaries to acquire an equity interest in the Company through the purchase of shares of Company common stock.

2. DEFINITIONS. As used herein, the following definitions shall apply:

(a) "Administrator" shall mean the entity, either the Board or the committee of the Board, responsible for administering this Plan, as provided in Section 3.

(b) "Board" shall mean the Board of Directors of the Company, as constituted from time to time.

(c) "Code" shall mean the Internal Revenue Code of 1986, as amended from time to time, and any successor statute.

(d) "Company" shall mean Advanced Polymer Systems, Inc., a Delaware corporation, and Participating Subsidiaries.

(e) "Common Stock" shall mean the Common Stock, \$.01 par value, of the Company.

(f) "Employee" shall mean any individual who is an employee of the Company or a Participating Subsidiary within the meaning of Section 3401(c) of the Code and the Treasury Regulations thereunder.

(g) "Enrollment Date" shall have the meaning set forth in Section 6.

(h) "Fair market value" means as of any given date: (i) the closing price of the Common Stock on the Nasdaq National Market as reported in the Wall Street Journal; or (ii) if the Common Stock is no longer quoted on the Nasdaq National Market, but is listed on an established stock exchange or quoted on any other established interdealer quotation system, the closing price for the Common Stock on such exchange or system, as reported in the Wall Street Journal; or (iii) in the absence of an established market for the Common Stock, the fair market value of the Common Stock as determined by the Administrator in good faith.

(i) "Lower Price Enrollment Date" shall have the meaning set forth in Section 6.

(j) "Option Period" shall have the meaning set forth in Section 7(b).

(k) "Participating Subsidiary" shall mean a Subsidiary which has been designated by the Administrator as covered by the Plan.

(l) "Plan" shall mean this Advanced Polymer Systems, Inc. 1997 Employee Stock Purchase Plan, as it may be amended from time to time.

(m) "Purchase Date" shall have the meaning set forth in Section 9(a).

(n) "Section" unless the context clearly indicates otherwise, shall refer to a Section of this Plan.

(o) "Subsidiary" shall mean a "subsidiary corporation" of the Company, whether now or hereafter existing, within the meaning of Section 424(f) of the Code, but only for so long as it is a "subsidiary corporation."

(p) "Trading Day" means any day on which regular trading occurs on any established stock exchange or market system on which the Common Stock is traded.

3. ADMINISTRATION.

(a) Administrator. The Plan shall be administered by the Board or, upon delegation by the Board, by a committee of the Board (in either case, the "Administrator"). In connection with the administration of the Plan, the Administrator shall have the powers possessed by the Board. The Administrator may act only by a majority of its members. The Administrator may delegate

administrative duties to such employees of the Company as it deems proper, so long as such delegation is not otherwise prohibited by Rule 16b-3 under the Securities Exchange Act of 1934, as amended, or other applicable law. The Board at any time may terminate the authority delegated to any committee of the Board pursuant to this Section 3(a) and revert in the Board the administration of the Plan.

(b) Administrator Determinations Binding. The Administrator may adopt, alter and repeal administrative rules, guidelines and practices governing the Plan and the options granted under it as it shall deem advisable from time to time, may interpret the terms and provisions of the Plan and the Options granted under it, may correct any defect, omission or inconsistency in the Plan or in any Option; and may otherwise supervise the administration of the Plan and the Options granted under it. The Administrator may establish, under guidelines from the Board, limits on the number of shares which may be purchased by each participant on an annual or other periodic basis or on the number of shares which may be purchased on any Purchase Date. All decisions made by the Administrator under the Plan shall be binding on all persons, including the Company and all participants in the Plan. No member of the Administrator shall be liable for any action that he or she has in good faith taken or failed to take with respect to this Plan.

4. NUMBER OF SHARES.

(a) The Company has reserved for sale under the Plan 800,000 shares of Common Stock. Shares sold under the Plan may be newly issued shares or shares reacquired in private transactions or open market purchases, but all shares sold under the Plan, regardless of source, shall be counted against the 800,000 share limitation. If at any Purchase Date, the shares available under the Plan are less than the number all participants would otherwise be entitled to purchase on such date, purchases shall be reduced proportionately to eliminate the deficit. If, at any Purchase Date, the shares which may be purchased by a participant are restricted on account of a limit on the aggregate shares which may be purchased per employee, purchases under each option shall be reduced proportionately. Any funds that cannot be applied to the purchase of shares due to such reductions shall be refunded to participants as soon as administratively feasible.

(b) In the event of any reorganization, recapitalization, stock split, reverse stock split, stock dividend, combination of shares, merger, consolidation, offering of rights, or other similar change in the capital structure of the Company, the Board may make such adjustment, if any, as it deems appropriate in the number, kind, and purchase price of the shares available for purchase under the Plan and in the maximum number of shares subject to any option under the Plan.

5. ELIGIBILITY REQUIREMENTS.

(a) Each Employee of the Company, except those described in the next paragraph, shall become eligible to participate in the Plan in accordance with Section 6 on the first Enrollment Date on or following commencement of his or her employment by the Company or following such period of employment as is designated by the Administrator from time to time. Participation in the Plan is entirely voluntary.

(b) The following Employees are not eligible to participate in the Plan:

(i) Employees who would, immediately upon enrollment in the Plan, own directly or indirectly, or hold options or rights to acquire stock possessing, five percent (5%) or more of the total combined voting power or value of all classes of stock of the Company or any subsidiary of the Company; and

(ii) Employees who are customarily employed by the Company fewer than twenty (20) hours per week or fewer than five (5) months in any calendar year.

6. ENROLLMENT. Any eligible employee may enroll or re-enroll in the Plan each year as of the close of the first trading day of: (a) May and November of each such year; or (b) such other days as may be established by the Board from time to time (the "Enrollment Dates"); provided, that the first Enrollment Date shall be April 30, 1997. In order to enroll, an eligible employee must complete, sign, and submit to the Company an enrollment form. Any enrollment form received by the Company by the 20th day of the month preceding an Enrollment Date (or by the Enrollment Date in the case of employees hired after such 20th day or in the case of the first Enrollment Date), or such other date established by the Administrator from time to time, will be effective on that Enrollment Date. In addition, the Administrator may re-enroll existing participants in the Plan on any Enrollment Date (the "Lower Price Enrollment Date") on which the fair market value of the Common Stock is lower than the fair market value on such participant's existing Enrollment

Date. A participant may elect not to re-enroll on a Lower Price Enrollment Date by filing a written statement with the Company declaring such election prior to the Lower Price Enrollment Date.

7. GRANT OF OPTION ENROLLMENT.

(a) Enrollment or re-enrollment by a participant in the Plan on an Enrollment Date will constitute the grant by the Company to the participant of an option to purchase shares of Common Stock from the Company under the Plan. Any participant whose option expires and who has not withdrawn from the Plan will automatically be re-enrolled in the Plan and granted a new option on the Enrollment Date immediately following the date on which the option expires.

(b) Except as provided in Section 10, each option granted under the Plan shall have the following terms:

(i) the option will have a term of not more than twenty-four (24) months or such shorter option period as may be established by the Board from time to time (the "Option Period"). Notwithstanding the foregoing, however, whether or not all shares have been purchased thereunder, the option will expire on the earlier to occur of: (A) the completion of the purchase of shares on the last Purchase Date occurring within twenty-four (24) months after the Enrollment Date for such option, or such shorter option period as may be established by the Board before an Enrollment Date for all options to be granted on such date; or (B) the date on which the employee's participation in the Plan terminates for any reason;

(ii) payment for shares purchased under the option will be made only through payroll withholding in accordance with Section 8;

(iii) purchase of shares upon exercise of the option will be effected only on the Purchase Dates established in accordance with Section 9;

(iv) the option, if not altered, amended or revoked by the Company prior to the relevant Purchase Date, may be accepted only by (x) there having been withheld from the compensation of the employee in accordance with the terms of the Plan amounts sufficient to purchase the Common Stock intended to be purchased under the option, and (y) the employee being employed by the Company and not having withdrawn from the Plan on the relevant Purchase Date.

(v) the price per share under the option will be determined as provided in Section 9;

(vi) the maximum number of shares available for purchase under an option for each one percent (1%) of compensation designated by an employee in accordance with Section 8 will, unless otherwise established by the Board before an Enrollment Date for all options to be granted on such date, be determined by dividing \$25,000 by the fair market value of a share of Common Stock on the Enrollment Date, dividing the result by the maximum number of percentage points that an employee may designate under Section 8 at the time such option is granted, and multiplying the result by the number of calendar years included in whole or in part in the period from grant to expiration of the option;

(vii) the option (taken together with all other options then outstanding under this and all other similar stock purchase plans of the Company and any subsidiary of the Company, collectively "Options") will in no event give the participant the right to purchase shares at a rate per calendar year which accrues in excess of \$25,000 of fair market value of such shares, less the fair market value of any shares accrued and already purchased during such year under Options which have expired or terminated, determined at the applicable Enrollment Dates; and

(viii) the option will in all respects be subject to the terms and conditions of the Plan, as interpreted by the Administrator from time to time.

8. PAYROLL AND TAX WITHHOLDING; USE BY COMPANY.

(a) Each participant shall elect to have amounts withheld from his or her compensation paid by the Company during the Option Period, at a rate equal to any whole percentage up to a maximum of ten percent (10%), or such lesser percentage as the Board may establish from time to time before an Enrollment Date. Compensation includes regular salary payments, annual and quarterly bonuses, hire-on bonuses, cash recognition awards, commissions, overtime pay, shift premiums, and elective contributions by the participant to qualified employee benefit plans, but excludes all other payments including, without limitation, long-term disability or workers compensation payments, car allowances, employee referral bonuses, relocation payments, expense

reimbursements (including but not limited to travel, entertainment, and moving expenses), salary gross-up payments, and non-cash recognition awards. The participant shall designate a rate of withholding in his or her enrollment form and may elect to increase or decrease the rate of contribution effective as of any Enrollment Date, by delivery to the Company, not later than ten (10) days before such Enrollment Date, of a written notice indicating the revised withholding rate.

(b) Payroll withholdings shall be credited to an account maintained for purposes of the Plan on behalf of each participant, as soon as administratively feasible after the withholding occurs. The Company shall be entitled to use the withholdings for any corporate purpose, shall have no obligation to pay interest on withholdings to any participant, and shall not be obligated to segregate withholdings.

(c) Upon disposition of shares acquired by exercise of an option, the participant shall pay, or make provision adequate to the Company for payment of, all federal, state, and other tax (and similar) withholdings that the Company determines, in its discretion, are required due to the disposition, including any such withholding that the Company determines in its discretion is necessary to allow the Company to claim tax deductions or other benefits in connection with the disposition. A participant shall make such similar provisions for payment that the Company determines, in its discretion, are required due to the exercise of an option, including such provisions as are necessary to allow the Company to claim tax deductions or other benefits in connection with the exercise of the option.

9. PURCHASE OF SHARES.

(a) On the last Trading Day immediately preceding an Enrollment Date (other than the first Enrollment Date), or on such other days as may be established by the Board from time to time prior to an Enrollment Date for all options to be granted on such Enrollment Date (each a "Purchase Date"), the Company shall apply the funds then credited to each participant's payroll withholdings account to the purchase of whole shares of Common Stock. The cost to the participant for the shares purchased under any option shall be not less than eighty-five percent (85%) of the lower of:

(i) the fair market value of the Common Stock on the Enrollment Date for such option; or

(ii) the fair market value of the Common Stock on the date such option is exercised.

(b) Any funds in an amount less than the cost of one share of Common Stock left in a participant's payroll withholdings account on a Purchase Date shall be carried forward in such account for application on the next Purchase Date.

(c) Notwithstanding the terms of Section 9(a), no funds credited to any employee's payroll withholdings account shall be used to purchase Common Stock on any date prior to the date that the Plan has been approved by the stockholders of the Company, as noted in Section 21. If such approval is not forthcoming within one year from the date that the Plan was approved by the Board of Directors, all amounts withheld shall be distributed to the participants as soon as administratively feasible.

10. WITHDRAWAL FROM THE PLAN. A participant may withdraw from the Plan in full (but not in part) at any time, effective after written notice thereof is received by the Company. Unless the Administrator elects to permit a withdrawing participant to invest funds credited to his or her withholding account on the Purchase Date immediately following notice of withdrawal, all funds credited to a participant's payroll withholdings account shall be distributed to him or her without interest within sixty (60) days after notice of withdrawal is received by the Company. Any eligible employee who has withdrawn from the Plan may enroll in the Plan again on any subsequent Enrollment Date in accordance with the provisions of Section 6.

11. TERMINATION OF EMPLOYMENT. Participation in the Plan terminates immediately when a participant ceases to be employed by the Company for any reason whatsoever (including death or disability) or otherwise becomes ineligible to participate in the Plan. As soon as administratively feasible after termination, the Company shall pay to the participant or his or her beneficiary or legal representative, all amounts credited to the participant's payroll withholdings account; provided, however, that if a participant ceases to be employed by the Company because of the commencement of employment with a Subsidiary of the Company that is not a Participating Subsidiary, funds then credited to such participant's payroll withholdings account shall be applied to the purchase of whole shares of Common Stock at the next Purchase Date and any funds remaining after such purchase shall be paid to the participant.

12. DESIGNATION OF BENEFICIARY.

(a) Each participant may designate one or more beneficiaries in the event of death and may, in his or her sole discretion, change such designation at any time. Any such designation shall be effective upon receipt in written form by the Company and shall control over any disposition by will or otherwise.

(b) As soon as administratively feasible after the death of a participant, amounts credited to his or her account shall be paid in cash to the designated beneficiaries or, in the absence of a designation, to the executor, administrator, or other legal representative of the participant's estate. Such payment shall relieve the Company of further liability with respect to the Plan on account of the deceased participant. If more than one beneficiary is designated, each beneficiary shall receive an equal portion of the account unless the participant has given express contrary written instructions.

13. ASSIGNMENT.

(a) The rights of a participant under the Plan shall not be assignable by such participant, by operation of law or otherwise. No participant may create a lien on any funds, securities, rights, or other property held by the Company for the account of the participant under the Plan, except to the extent that there has been a designation of beneficiaries in accordance with the Plan, and except to the extent permitted by the laws of descent and distribution if beneficiaries have not been designated.

(b) A participant's right to purchase shares under the Plan shall be exercisable only during the participant's lifetime and only by him or her, except that a participant may direct the Company in the enrollment form to issue share certificates to the participant and his or her spouse in community property, to the participant jointly with one or more other persons with right of survivorship, or to certain forms of trusts approved by the Administrator.

14. ADMINISTRATIVE ASSISTANCE. If the Administrator in its discretion so elects, it may retain a brokerage firm, bank, or other financial institution to assist in the purchase of shares, delivery of reports, or other administrative aspects of the Plan. If the Administrator so elects, each participant shall (unless prohibited by the laws of the nation of his or her employment or residence) be deemed upon enrollment in the Plan to have authorized the establishment of an account on his or her behalf at such institution. Shares purchased by a participant under the Plan shall be held in the account in the name in which the share certificate would otherwise be issued pursuant to Section 13(b).

15. COSTS. All costs and expenses incurred in administering the Plan shall be paid by the Company, except that any stamp duties or transfer taxes applicable to participation in the Plan may be charged to the account of such participant by the Company. Any brokerage fees for the purchase of shares by a participant shall be paid by the Company, but brokerage fees for the resale of shares by a participant shall be borne by the participant.

16. EQUAL RIGHTS AND PRIVILEGES. All eligible employees shall have equal rights and privileges with respect to the Plan so that the Plan qualifies as an "employee stock purchase plan" within the meaning of Section 423 of the Code and the related Treasury Regulations. Any provision of the Plan which is inconsistent with Section 423 of the Code shall without further act or amendment by the Company or the Board be reformed to comply with the requirements of Section 423. This Section 16 shall take precedence over all other provisions of the Plan.

17. APPLICABLE LAW. The Plan shall be governed by the substantive laws (excluding the conflict of laws rules) of the State of California.

18. MODIFICATION AND TERMINATION.

(a) The Board may amend, alter, or terminate the Plan at any time, including amendments to outstanding options. No amendment shall require stockholder approval, except:

(i) for an increase in the number of shares reserved for purchase under the Plan;

(ii) to the extent required for the Plan to comply with Section 423 of the Code;

(iii) to the extent required by other applicable laws, regulations or rules; or

(iv) to the extent the Board otherwise concludes that stockholder approval is advisable.

(b) In the event the Plan is terminated, the Board may elect to terminate all outstanding options either immediately or upon completion of the purchase of shares on the next Purchase Date, or may elect to permit options to expire in accordance with their terms (and participation to continue through such expiration dates). If the options are terminated prior to expiration, all funds contributed to the Plan that have not been used to purchase shares shall be returned to the participants as soon as administratively feasible.

(c) In the event of the sale of all or substantially all of the assets of the Company, or the merger of the Company with or into another corporation, or the dissolution or liquidation of the Company, each option outstanding under the Plan shall be assumed by any purchaser of all or substantially all of the assets of the Company or by a successor by merger to the Company (or the parent company of such purchaser or successor) in compliance with Section 424 of the Code, unless otherwise provided by the Board in its sole discretion, in which event, a Purchase Date shall occur immediately before the effective date of such event.

19. RIGHTS AS AN EMPLOYEE. Nothing in the Plan shall be construed to give any person the right to remain in the employ of the Company or to affect the Company's right to terminate the employment of any person at any time with or without cause.

20. RIGHTS AS A SHAREHOLDER; DELIVERY OF CERTIFICATES. Unless otherwise determined by the Board, certificates evidencing shares purchased on any Purchase Date shall be delivered to a participant only if he or she makes a written request to the Administrator. Participants shall be treated as the owners of their shares effective as of the Purchase Date.

21. BOARD AND SHAREHOLDER APPROVAL. The Plan was approved by the Board of Directors on March 5, 1997, and by the holders of a majority of the votes cast at a duly held shareholders' meeting on June 18, 1997, at which a quorum of the voting power of the Company was represented in person or by proxy.

Amended by the Board on: March 25, 2004

Approved by the stockholders on: May 25, 2004

Effective date of this Plan: March 25, 2004

Amended by the Board on: January 11, 2005

Approved by the stockholders on: May 25, 2005

Effective date of this Plan: January 11, 2005

Amended by the Board on: January 10, 2006

Approved by the stockholders on:

Effective date of this Plan:
