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

FORM 8-K

CURRENT REPORT

Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

Date of Report (Date of earliest event reported) April 24, 2011

A.P. Pharma, Inc.

(Exact name of registrant as specified in its charter)

Delaware	**001-33221**	**94-2875566**
(State or other jurisdiction of incorporation)	**(Commission File Number)**	**(I.R.S. Employer Identification No.)**

123 Saginaw Drive Redwood City CA	**94063**
(Address of principal executive offices)	**(Zip Code)**

Registrant's telephone number, including area code (650) 366-2626

N/A
(Former name or former address, if changed since last report)

Check the appropriate box below if the Form 8-K filing is intended to simultaneously satisfy the filing obligation of the registrant under any of the following provisions (see General Instruction A.2. below):

☐ Written communications pursuant to Rule 425 under the Securities Act (17 CFR 230.425)

☐ Soliciting material pursuant to Rule 14a-12 under the Exchange Act (17 CFR 240.14a-12)

☐ Pre-commencement communications pursuant to Rule 14d-2(b) under the Exchange Act (17 CFR 240.14d-2(b))

☐ Pre-commencement communications pursuant to Rule 13e-4(c) under the Exchange Act (17 CFR 240.13e-4(c))

Item 1.01 Entry Into A Material Definitive Agreement

Securities Purchase Agreement

On April 24, 2011, A.P. Pharma, Inc. (the "Company") entered into a Securities Purchase Agreement (the "Purchase Agreement") with the purchasers named therein (the "Purchasers"). Pursuant to the Purchase Agreement, the Company may issue up to $4.5 million aggregate principal amount of senior secured convertible notes due 2021 (the "Notes") that are convertible into shares (the "Conversion Shares") of the Company's common stock, par value $0.01, subject to the satisfaction of closing conditions. The Company will receive $1.5 million at an initial closing that is expected to take place on April 29, 2011, or at such other time the Company and the Purchasers may agree (the "Initial Closing Date"). The Purchasers may also purchase up to an additional $3.0 million aggregate principal amount of Notes from time to time, with such right expiring upon the second anniversary of the Initial Closing Date.

The Notes are secured by substantially all of the assets of the Company. The Notes bear interest at 20% per annum, payable quarterly in cash or in additional principal amount of Notes at the election of the Purchasers. The Notes are convertible into Conversion Shares at a conversion rate of 25,000 shares per $1,000 principal amount of Notes. The conversion rate will be adjusted for certain customary events. There is no right to convert the Notes to the extent that after giving effect to such conversion the holder (together with such holder's affiliates) would beneficially own in excess of 9.99% (the "Maximum Percentage") of the number of shares of common stock of the Company outstanding immediately after giving effect to such conversion. Each holder of the Notes can increase or decrease the Maximum Percentage for such holder's Notes by written notice to the Company, provided that such increase or decrease will not be effective until 61 days after delivery of the notice. Under the Notes, certain events are considered "Events of Default," which will allow a Purchaser to require the Company to redeem all or any portion of its Notes, including:

- the Company's failure to satisfy its conversion obligations on any of the Notes upon the exercise of a Purchaser's conversion right on such Notes provided that such failure continues for a period of 10 business days;
- the Company's failure to pay the principal on any of the Notes, any interest due under the Notes or any other amounts due under other agreements delivered in connection with this transaction, provided that in the case of failed interest payments, such failure continues for a period of five business days;
- the Company's failure to comply with any other term, covenant or agreement contained in the Purchase Agreement provided that such failure is not cured within 10 business days;
- any representation or warranty made by the Company in the Purchase Agreement shall prove to be materially false or misleading as of the date made or deemed made;
- default by the Company in any payment when due under any indebtedness in an aggregate principal amount of $100,000;
- default by the Company under any material contract, as such term is defined in the Purchase Agreement;
- the Security Agreement (as defined below) ceases to create a valid and perfected lien of the collateral;
- the failure of the respective Registration Statements (as defined below) to be declared effective by the Securities and Exchange Commission (the "SEC") on or prior to the date that is 60 days after the applicable Effectiveness Deadline (as defined in the Purchase Agreement), or, while the applicable Registration Statement is required to be maintained effective pursuant to the terms of the Purchase Agreement, the effectiveness of the applicable Registration Statement lapses for any reason or is unavailable to any holder of the Notes for sale of all of such holder's Conversion Shares, and such lapse or unavailability continues for a period of 20 consecutive days or for more than an aggregate of 45 days in any 365-day period, subject to certain grace periods; and
- certain events of bankruptcy or insolvency with respect to the Company.

Pursuant to the Purchase Agreement, the Company agreed to file within 30 days of the Initial Closing Date (i) a registration statement on Form S-1 with the SEC to register the offer and sale of up to $20.0 million of equity securities to be offered and sold by the Company on a primary basis (the "Follow-on Registration Statement") and (ii) a registration statement on Form S-3 with the SEC covering the resale of the full amount of the Conversion Shares (the "Resale Registration Statement" and together with the Follow-on Registration Statement, the "Registration Statements"). The Company agreed to use its commercially reasonable efforts to cause the Follow-on Registration Statement to be declared effective by the SEC as promptly as practicable and the Resale Registration Statement to be declared effective by the SEC within 90 days after the Initial Closing Date (or 120 days in the event the Resale Registration Statement is reviewed by the SEC). If the Company fails to meet certain filing or effectiveness deadlines with respect to the Registration Statements or fails to keep any Registration Statement continuously effective (with limited exceptions), the Company may be obligated to pay to the holders of the Conversion Shares liquidated damages in the amount of 2% per month of such holder's pro rata interest in the total purchase price of the Notes. In the event the Company fails to pay such liquidated damages in a timely manner, the damages will bear interest at the rate of 2% per month (prorated for partial months) until paid in full.

In connection with the Purchase Agreement, the Company and Tang Capital Partners, LP, in its capacity as representative of the Purchasers (the "Agent"), entered into a Security Agreement dated April 24, 2011 (the "Security Agreement"), pursuant to which the Company granted to the Agent a security interest in substantially all of its assets.

The financing is exempt from registration pursuant to the exemption for transactions by an issuer not involving any public offering under Section 4(2) the Securities Act of 1933, as amended (the "Securities Act"), and Regulation D under the Securities Act.

The securities sold and issued in connection with the Purchase Agreement have not been registered under the Securities Act or any state securities laws and may not be offered or sold in the United States absent registration with the SEC or an applicable exemption from the registration requirements.

The foregoing description of the transaction is only a summary and is qualified in its entirety by reference to the Purchase Agreement, the Form of Note and the Security Agreement, copies of which are filed as Exhibits 10.1, 10.2 and 10.3 hereto, respectively.

Lease Amendment

On April 25, 2011, the Company entered into the Second Amendment to Lease (the "Lease Amendment") with Metropolitan Life Insurance Company, effective as of April 1, 2011, pursuant to which the Company extended the lease for its offices through September 30, 2011. A copy of the Lease Amendment is filed as Exhibit 10.4 hereto.

Item 3.02 Unregistered Sales of Equity Securities

The information called for by this item is contained in Item 1.01, which is incorporated herein by reference.

Item 3.03 Material Modification to Rights of Security Holders

In order to enable the transaction described in Item 1.01 above, on April 24, 2011, the Board of Directors of the Company (the "Board") approved the termination of the Company's Preferred Shareholders Rights Agreement with Computershare Trust Company N.A. dated as of December 18, 2006, as amended (the "Rights Agreement"), effective immediately prior to the Initial Closing Date. Under the Rights Agreement, preferred stock purchase rights (the "Rights") were distributed to stockholders of record as of January 2, 2007 (and to each person who acquires the Company's common stock after that date unless determined otherwise by the board of directors) at the rate of one Right for each share of common stock held. The Rights were exercisable only upon the acquisition, or the acquisition of the right to acquire, by a

person or group of affiliated or associated persons, of 20% or more (34% for Tang Capital Partners, LP and 30% for Baker Brothers Investments) of the outstanding shares of the Company's common stock. Once exercisable, each Right would have entitled the holder to purchase, at a price of $44.00, one one-thousandth of a share of the Company's Series A Participating Preferred Stock. As a result of the termination of the Rights Agreement, all Rights will be terminated. The Rights Agreement had not been triggered to date.

ITEM 5.02 Departure of Directors or Certain Officers; Election of Directors; Appointment of Certain Officers; Compensatory Arrangements of Certain Officers

On April 24, 2011, the Board appointed John B. Whelan as President, Chief Executive Officer and Director, effective immediately. Mr. Whelan has been with A.P. Pharma since February 2009, serving most recently as Acting Chief Executive Officer and Chief Financial Officer and previously as Vice President of Finance and Chief Financial Officer. He was Chief Operating Officer and Chief Financial Officer at Raven biotechnologies, inc., a private company developing antibody-based cancer therapeutics, from April 2002 until the company's acquisition in July 2008. From January 2000 to March 2002, he was Vice President and Chief Financial Officer at Eos Biotechnology, Inc., a private therapeutic antibodies company. Mr. Whelan's qualifications to serve on the Board include his management experience with the Company, which gives him valuable insight into the operations of the Company, and his former executive management positions with other biotechnology companies.

In connection with Mr. Whelan's appointment, the Company entered into a management retention agreement with Mr. Whelan on April 25, 2011 (the "Whelan Management Agreement"). The Whelan Management Agreement provides that if Mr. Whelan's employment is terminated by the Company not in connection with a change of control, without cause, as such term is defined in the Whelan Management Agreement, or by Mr. Whelan as a result of certain events set forth in the Whelan Management Agreement, during the 12 months after the date of termination (the "Severance Period"), he shall receive (i) an amount equal to the monthly base salary he was receiving immediately prior to the termination, (ii) the average bonus paid during each of the three 12-month periods (or such shorter period of time during which he was eligible for a bonus) prior to termination, and (iii) the immediate vesting of unvested stock options, restricted stock and other equity awards that otherwise would have vested during the Severance Period. The Company also agreed to reimburse for or continue to pay for health care benefits during the Severance Period, or such date when he is no longer eligible for such benefits under applicable law. In the event Mr. Whelan's employment is terminated by the Company without good cause or he resigns for good reason within 12 months following a change of control of the Company, then in lieu of the above benefits, during the 18-month period after the date of termination (the "Change of Control Severance Period"), he shall receive (i) an amount equal to the greater of (A) the base salary he was receiving immediately prior to the termination or (B) the base salary he was receiving immediately prior to the change of control, (ii) 150% of the average bonus paid during each of the three 12-month periods (or such shorter period of time during which he was eligible for a bonus) prior to termination, and (iii) the immediate vesting of unvested stock options, restricted stock and other equity awards. The Company also agreed to reimburse for or continue to pay for health care benefits during the Change of Control Severance Period, or such date when he is no longer eligible for such benefits under applicable law. A copy of the Whelan Management Agreement is filed as Exhibit 10.5 hereto.

In addition, on April 24, 2011, the Board appointed Michael A. Adam, Ph.D., as Senior Vice President and Chief Operating Officer, effective immediately. Dr. Adam has been working with the Company as a consultant since July 2010. From October 2008 to June 2010, he was Senior Vice President of Pharmaceutical Operations at Spectrum Pharmaceuticals, Inc., a biotechnology company with fully integrated commercial and drug development operations with a primary focus in oncology. From March 2006 to February 2007, Dr. Adam served as Vice President, Drug Development Operations at Anadys Pharmaceuticals, Inc., a biopharmaceutical company dedicated to improving patient care by developing novel medicines for the treatment of hepatitis C. Prior to that, Dr. Adam held various senior positions with Pfizer, Inc., Agouron Pharmaceuticals, Inc. and Bristol-Myers Squibb Company. Dr. Adam received his Ph.D. in organic chemistry at the Massachusetts Institute of Technology.

In connection with Dr. Adam's appointment, the Company entered into a management retention agreement with Dr. Adam on April 25, 2011 (the "Adam Management Agreement"). The Adam Management Agreement provides that if Dr. Adam's employment is terminated by the Company not in connection with a change of control, without cause, as such term is defined in the Adam Management Agreement, or by Dr. Adam as a result of certain events set forth in the Adam Management Agreement, during the six months after the date of termination (the "Severance Period"), he shall receive (i) an amount equal to the monthly base salary he was receiving immediately prior to the termination, (ii) one-half the average bonus paid during each of the three 12-month periods (or such shorter period of time during which he was eligible for a bonus) prior to termination, and (iii) the immediate vesting of unvested stock options, restricted stock and other equity awards that otherwise would have vested during the Severance Period. The Company also agreed to reimburse for or continue to pay for health care benefits during the Severance Period, or such date when he is no longer eligible for such benefits under applicable law. In the event Dr. Adam's employment is terminated by the Company without good cause or he resigns for good reason within 12 months following a change of control of the Company, then in lieu of the above benefits, during the twelve months after the date of termination (the "Change of Control Severance Period"), he shall receive (i) an amount equal to the greater of (A) the monthly base salary he was receiving immediately prior to the termination or (B) the base salary he was receiving immediately prior to the change of control, (ii) the average bonus paid during each of the three 12-month periods (or such shorter period of time during which he was eligible for a bonus) prior to termination, and (iii) the immediate vesting of unvested stock options, restricted stock and other equity awards. The Company also agreed to reimburse for or continue to pay for health care benefits during the Change of Control Severance Period, or such date when he is no longer eligible for such benefits under applicable law. A copy of the Adam Management Agreement is filed as Exhibit 10.6 hereto.

Item 8.01 Other Events

On April 25, 2011, the Company issued the press release attached hereto as Exhibit 99.1 regarding the transaction and management changes described in Item 1.01 and Item 5.02 this report, respectively.

Item 9.01 Financial Statements and Exhibits.

(d) Exhibits. The following material is filed as an exhibit to this Current Report on Form 8-K:

10.1 Securities Purchase Agreement, dated as of April 24, 2011, by and among the Company and the purchasers listed therein.

10.2 Form of Senior Secured Convertible Note due 2021.

10.3 Security Agreement, dated as of April 24, 2011, by and between the Company and Tang Capital Partners, LP, as Agent for the Purchasers.

10.4 Second Amendment to Lease, effective as of April 1, 2011, by and between the Company and Metropolitan Life Insurance Company.

10.5 Management Retention Agreement, dated as of April 25, 2011, by and between the Company and John B. Whelan.

10.6 Management Retention Agreement, dated as of April 25, 2011, by and between the Company and Michael A. Adam.

99.1 Press Release of A.P. Pharma, Inc. dated April 25, 2011.

SIGNATURE

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

A.P. Pharma, Inc.

Date: April 28, 2011

/s/ John B. Whelan

John B. Whelan
President, Chief Executive Officer and Chief Financial Officer

EXHIBIT INDEX

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SECURITIES PURCHASE AGREEMENT

AMONG

A.P. PHARMA, INC.,

TANG CAPITAL PARTNERS, LP,

BAKER BROS. INVESTMENTS II, L.P.,

BAKER BROTHERS LIFE SCIENCES, L.P.,

AND

14159, L.P.

DATED AS OF APRIL 24, 2011

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LIST OF EXHIBITS

SECURITIES PURCHASE AGREEMENT

This SECURITIES PURCHASE AGREEMENT (this "***Agreement***") is made and entered into as of April 24, 2011 by and among A.P. Pharma, Inc., a Delaware corporation (the "***Company***"), Tang Capital Partners, LP, a Delaware limited partnership, Baker Bros. Investments II, L.P., a Delaware limited partnership, Baker Brothers Life Sciences, L.P., a Delaware limited partnership and 14159, L.P., a Delaware limited partnership (each a "***Purchaser***" and together the "***Purchasers***"). Certain terms used and not otherwise defined in the text of this Agreement are defined in Section 12 hereof.

RECITALS

WHEREAS, the Company and the Purchasers are executing and delivering this Agreement in reliance upon the exemption from securities registration afforded by Section 4(2) of the Securities Act of 1933, as amended (the "***Securities Act***"), and Rule 506 of Regulation D ("***Regulation D***") as promulgated by the United States Securities and Exchange Commission (the "***Commission***) under the Securities Act;

WHEREAS the Company has authorized a new series of Senior Secured Convertible Notes due 2021 (the "***Notes***"), in the form attached hereto as Exhibit A, which Notes shall be convertible into the Company's common stock, $0.01 par value per share (the "***Common Stock***"), and, in accordance with the terms of the Notes, the interest on the Notes may be payable through the addition of the amount of such Interest to the then outstanding principal ("***PIK Interest***");

WHEREAS the Company desires to sell to the Purchasers, and the Purchasers desire to purchase from the Company, Notes of the Company, all in accordance with the terms and provisions of this Agreement; and

WHEREAS, the Purchasers have committed to investing a minimum aggregate amount of $1,500,000 (the "***Commitment Amount***") in the transactions as described herein;

NOW, THEREFORE, in consideration of the foregoing and the mutual representations, warranties and covenants herein contained, the parties hereto hereby agree as follows:

1. Authorization of Securities. The Company has authorized the issuance and sale of Notes, in an aggregate principal amount of up to $4,500,000, without regard to amounts potentially payable as PIK Interest. Each Note shall be in the form of Exhibit A attached hereto, shall be duly executed by the Company and shall be dated as of the date of the applicable Closing (as defined in Section 3.1). The Notes will be senior in right of payment to any future indebtedness, and secured by substantially all of the assets of the Company pursuant to the Security Agreement, in the form of Exhibit B hereto (the "***Security Agreement***"), which shall be duly executed by the Company and the Purchasers as of the date hereof. The shares of Common Stock into which the Notes are convertible are sometimes referred to herein as the "***Conversion Shares***", and the Notes (including any PIK Interest that may be paid thereon) and the Conversion Shares are sometimes referred to herein collectively as the "***Securities***."

2. Sale and Purchase of the Securities. Upon the terms and subject to the conditions herein contained, the Company agrees to sell to each Purchaser, and each Purchaser agrees to purchase from the Company, at the Initial Closing (as defined in Section 3.1) that amount of face value of Notes as set forth on Schedule I attached hereto for a corresponding purchase price to be paid in cash, resulting in aggregate proceeds of $1,500,000 (the "***Note Purchase Price***").

3. Closing; Payment of Purchase Price; Use of Proceeds.

3.1. Closings.

(a) The initial closing (the "***Initial Closing***"), with respect to the transaction contemplated in Section 2 hereof, shall take place at the offices of Ropes & Gray LLP, Three Embarcadero Center, San Francisco, California on April 29, 2011, or at such other time and place as the Company and Purchasers may agree, including remotely via the exchange of documents and signatures (the "***Initial Closing Date***"). If the Initial Closing Date does not occur within seven business days from the date hereof, a majority in interest of the Purchasers, in their sole discretion, may terminate this Agreement.

(b) The term "***Closing***" shall refer to the Initial Closing and each Subsequent Closing (as defined in Section 3.2), to the extent there is a Subsequent Closing. At the Initial Closing, the Company shall issue to each Purchaser a Note representing the principal amount which such Purchaser is purchasing at the Closing, in the name of such Purchaser, against delivery to the Company by that Purchaser of a wire transfer in the amount of the Note Purchase Price therefor.

3.2. Subsequent Closings. At any time and from time to time from and after the Initial Closing, each Purchaser may elect to purchase up to its Pro Rata Interest in an additional $3,000,000 aggregate principal amount of Notes ("***Additional Notes***") at a price equal to such additional principal amount; provided, the right to purchase Additional Notes shall expire upon the second anniversary of the Initial Closing Date. A Purchaser electing to purchase Additional Notes shall provide at least two (2) days' notice to the Company of such election, with each such closing (each a "***Subsequent Closing***") to occur at the offices of Ropes & Gray LLP, Three Embarcadero Center, San Francisco, California, on the date and time elected by such Purchaser or at such other time and place as the Company and Purchasers may agree, including remotely via the exchange of documents and signatures (each a "***Subsequent Closing Date***" and together with the Initial Closing Date, each a "***Closing Date***"). At each Subsequent Closing, the Company shall provide a certification that the conditions set forth in Section 7.1 continue to be satisfied with respect to the Additional Notes to be purchased in such Closing.

4. Representations and Warranties of the Purchasers; Register of Securities; Restrictions on Transfer. Each Purchaser, severally but not jointly, represents and warrants to the Company that the statements contained in this Section 4 are true and complete as of the date of this Agreement and will be true and complete as of the date of each Closing:

4.1. Organization. The Purchaser represents that the Purchaser is duly formed, validly existing and in good standing under the laws of Delaware, has not been organized, reorganized or recapitalized specifically for the purpose of investing in the Company and has all

partnership power and authority to enter into this Agreement and the other Transaction Documents and instruments referred to herein to which it is a party and to consummate the transactions contemplated hereby and thereby.

4.2. Validity. The execution, delivery and performance of this Agreement, and the other Transaction Documents and instruments referred to herein, in each case to which the Purchaser is a party, and the consummation by the Purchaser of the transactions contemplated hereby and thereby, have been duly authorized by all necessary action on the part of the Purchaser. This Agreement has been duly executed and delivered by the Purchaser, and the other Transaction Documents and instruments referred to herein to which it is a party will be duly executed and delivered by the Purchaser, and each such agreement and instrument constitutes or will constitute a valid and binding obligation of the Purchaser, enforceable against it in accordance with its terms, except as limited by applicable bankruptcy, insolvency, reorganization, moratorium, fraudulent conveyance, and any other laws of general application affecting enforcement of creditors' rights generally, and as limited by laws relating to the availability of specific performance, injunctive relief, or other equitable remedies.

4.3. Brokers. There is no broker, investment banker, financial advisor, finder or other Person which has been retained by or is authorized to act on behalf of the Purchaser who might be entitled to any fee or commission for which the Company will be liable in connection with the execution of this Agreement and the consummation of the transactions contemplated hereby.

4.4. Investment Representations and Warranties. The Purchaser understands and agrees that the offering and sale of the Securities has not been registered under the Securities Act or any applicable state securities laws and is being made in reliance upon federal and state exemptions for transactions not involving a public offering which depend upon, among other things, the bona fide nature of the investment intent and the accuracy of the Purchaser's representations as expressed herein.

4.5. Investor Questionnaire. In connection with the filing of a Registration Statement, the Company may require the Purchaser to furnish to the Company such information regarding the Purchaser and the Registrable Securities, as the Company may reasonably request in writing and as shall reasonably be required in connection with the filing of the Registration Statement. At least five (5) Business Days prior to the first anticipated filing date of such Registration Statement, the Company shall notify the Purchaser of the information the Company requests from the Purchaser.

4.6. Acquisition for Own Account. The Purchaser is acquiring the Securities for its own account for investment and not with a view toward distribution in a manner which would violate the Securities Act or any applicable state securities laws.

4.7. Ability to Protect Its Own Interests and Bear Economic Risks. The Purchaser, by reason of the business and financial experience of its management, has the capacity to protect its own interests in connection with the transactions contemplated by this Agreement and the other Transaction Documents and is capable of evaluating the merits and risks of the investment in the Securities. The Purchaser is able to bear the economic risk of an

investment in the Securities and is able to sustain a loss of all of its investment in the Securities without economic hardship, if such a loss should occur.

4.8. Accredited Investor. The Purchaser is an "accredited investor" as that term is defined in Regulation D promulgated under the Securities Act.

4.9. Access to Information. The Purchaser has been given access to all Company documents, records, and other information, and has had adequate opportunity to ask questions of, and receive answers from, the Company's officers, employees, agents, accountants, and representatives concerning the Company's business, operations, financial condition, assets, liabilities, and all other matters relevant to its investment in the Securities. The foregoing, however, does not limit or modify the representations and warranties made by the Company pursuant to Section 5 of this Agreement or the right of the Purchaser to rely thereon.

4.10. Restricted Securities.

(a) The Purchaser understands that the Securities will be characterized as "restricted securities" under the federal securities laws inasmuch as they are being acquired from the Company in a private placement under Section 4(2) of the Securities Act and that under such laws and applicable regulations such Securities may be resold without registration under the Securities Act only in certain limited circumstances.

(b) The Purchaser acknowledges that the Securities must be held indefinitely unless subsequently registered under the Securities Act and under applicable state securities laws or an exemption from such registration is available. The Purchaser understands that the Company is under no obligation to register the Securities, except as provided in the Transaction Documents.

(c) The Purchaser is aware of the provisions of Rule 144 under the Securities Act which permit limited resale of securities purchased in a private placement.

4.11. Tax Advisors. The Purchaser has had the opportunity to review with the Purchaser's own tax advisors the federal, state and local tax consequences of this investment, where applicable, and the transactions contemplated by this Agreement. The Purchaser is relying solely on the Purchaser's own determination as to tax consequences or the advice of such tax advisors and not on any statements or representations of the Company or any of its agents and understands that the Purchaser (and not the Company) shall be responsible for the Purchaser's own tax liability that may arise as a result of this investment or the transactions contemplated by this Agreement.

4.12. Communication of Offer. The offer to sell the Securities was directly communicated to the Purchaser by the Company. At no time was the Purchaser presented with or solicited by any leaflet, advertisement, article, notice or other communication published in any newspaper, magazine, or similar media or broadcast over television or radio, or any other form of general advertising, or solicited or invited to attend a promotional meeting or any seminar or meeting by any general solicitation or general advertising.

4.13. Short Sales, etc. Purchaser represents, warrants and covenants to the Company that Purchaser has not, either directly or indirectly through an affiliate, agent or representative of the Company, engaged in any transaction in the securities of the Company during the thirty (30) days prior to the date hereof, except as set forth in filings made with the Commission pursuant to Section 16 of the Exchange Act. Purchaser represents and warrants to and covenants with the Company that Purchaser has not, during the thirty (30) days prior to the date hereof, engaged and will not engage in any short sales of the Company's Common Stock prior to the effectiveness of the Registration Statement (either directly or indirectly through an affiliate, agent or representative).

5. Representations and Warranties by the Company. Except as disclosed by the Company in a written Disclosure Schedule provided by the Company to the Purchasers dated the date hereof (the ***"Disclosure Schedule***"), the Company represents and warrants to the Purchasers that the statements contained in this Section 5 are true and complete as of the date of this Agreement and will be true and complete as of the date of the Initial Closing and the Subsequent Closings, as the case may be. The Disclosure Schedule shall be arranged in sections corresponding to the numbered and lettered sections and subsections contained in this Section 5, and the disclosures in any section or subsection of the Disclosure Schedule shall qualify other sections and subsections in this Section 5 only to the extent it is clear from a reasonable reading of the disclosure that such disclosure is applicable to such other sections and subsections.

5.1. Capitalization.

(a) As of the date hereof, without giving effect to any of the Closings, the authorized capital stock of the Company consists of 100,000,000 shares of Common Stock, par value $0.01 per share, and 2,500,000 shares of preferred stock, par value $0.01 per share ("***Preferred Stock***"). As of the date hereof, there are 40,064,194 shares of Common Stock issued and outstanding and no shares of Preferred Stock issued and outstanding. The Company has reserved 109,158 shares of Common Stock for issuance to employees of the Company pursuant to its 1997 Employee Stock Purchase Plan (the "***ESPP***"). The Company has reserved 3,944,597 shares of Common Stock for issuance to employees, officers, directors and consultants of the Company pursuant to its 2007 Equity Incentive Plan, as amended and in effect, duly adopted by the Board of Directors of the Company (the "***Board of Directors***") and approved by the stockholders of the Company ("***2007 Equity Incentive Plan***"). Of such reserved shares of Common Stock for the 2007 Equity Incentive Plan, options to purchase 1,898,305 shares of Common Stock have been granted and are currently outstanding, 1,013,805 shares of Common Stock have been granted as restricted stock awards and are currently outstanding and 2,046,292 shares of Common Stock remain available for issuance to employees, officers, directors and consultants pursuant to the 2007 Equity Incentive Plan. The Company has reserved 325,533 shares of Common Stock for issuance to employees, officers, directors and consultants of the Company pursuant to its 2002 Stock Incentive Plan, as amended and in effect, duly adopted by the Board of Directors and approved by the stockholders of the Company ("***2002 Stock Incentive Plan***"). Of such reserved shares of Common Stock for the 2002 Stock Incentive Plan, options to purchase 246,742 shares of Common Stock have been granted, 163,496 shares of Common Stock have been granted as restricted stock awards and are currently outstanding and 78,791 shares of Common Stock remain

available for issuance to employees, officers, directors and consultants pursuant to the 2002 Stock Incentive Plan. The Company has reserved 1,028,958 shares of Common Stock for issuance to employees, officers, directors and consultants of the Company pursuant to its Non-Qualified Stock Plan, as amended and in effect, duly adopted by the Board of Directors and approved by the stockholders of the Company (the "***Non-Qualified Stock Plan***"). Of such reserved shares of Common Stock for the Non-Qualified Stock Plan, options to purchase 1,028,958 shares of Common Stock have been granted, 0 shares of Common Stock have been granted as restricted stock awards and are currently outstanding and 0 shares of Common Stock remain available for issuance to prospective employees and non-executive employees and consultants pursuant to the Non-Qualified Stock Plan. The Company has reserved 200,000 shares of Preferred Stock for issuance upon the exercise of the rights pursuant to the Preferred Shareholders Rights Agreement, as amended and in effect, duly adopted by the Board of Directors and approved by the Company stockholders (the "***Preferred Shareholders Rights Agreement***"). The Company has no other shares of capital stock authorized, issued or outstanding. A capitalization table presenting the capitalization of the Company as of the date hereof, without giving effect to any of the Closings, is set forth on Schedule 5.1(a) hereto. At each Subsequent Closing, if any, the Company shall provide an updated capitalization table representing the capitalization of the Company on such date thereof.

(b) As of the date hereof, after giving effect to the Initial Closing and the Subsequent Closings, if any, except as may be granted by this Agreement and the other Transaction Documents, (i) other than as set forth in Schedule 5.1(b), there are no outstanding options, warrants, scrip, rights to subscribe to, calls or commitments of any character whatsoever relating to, or securities or rights convertible into or exercisable or exchangeable for, any shares of capital stock of the Company, or arrangements by which the Company is or may become bound to issue additional shares of capital stock, nor are any such issuances or arrangements contemplated other than pursuant to the ESPP, 2007 Equity Incentive Plan, 2002 Stock Incentive Plan, the Non-Qualified Stock Plan and the Preferred Shareholders Rights Agreement; (ii) other than as set forth in Schedule 5.1(b), there are no agreements or arrangements under which the Company is or may become obligated to register the sale of any of its securities under the Securities Act; (iii) the Company has no obligation (contingent or otherwise) to purchase, redeem or otherwise acquire any of its equity securities or any interests therein or to pay any dividend or make any distribution in respect thereof, except as required by the Charter Documents; and (iv) except for 109,158 shares of Common Stock reserved for issuance under the ESPP, 3,944,597 shares of Common Stock reserved under the 2007 Equity Incentive Plan, 325,533 shares of Common Stock reserved under the 2002 Stock Incentive Plan, 1,028,958 shares of Common Stock reserved under the Non-Qualified Stock Plan and 200,000 shares of Preferred Stock reserved under the Preferred Shareholder Rights Agreement as set forth in Schedule 5.1(b) hereto, the Company has not reserved any shares of capital stock for issuance pursuant to any stock option plan or similar arrangement.

5.2. Due Issuance and Authorization of Capital Stock. All of the outstanding shares of capital stock of the Company have been validly issued and are fully paid and non-assessable. The issuance of the Conversion Shares to the Purchasers pursuant to the terms hereof

upon conversion of the Notes will vest in the holders thereof legal and valid title to such Conversion Shares, free and clear of any lien, claim, judgment, charge, mortgage, security interest, pledge, escrow, equity or other encumbrance other than restrictions pursuant to any applicable state or federal securities laws (collectively, ***"Encumbrances***").

5.3. Organization. The Company (a) is duly incorporated or otherwise organized, validly existing and in good standing under the laws of the jurisdiction of its formation, (b) is duly qualified to do business as a foreign entity and is in good standing in each jurisdiction where the nature of the property owned or leased by it or the nature of the business conducted by it makes such qualification necessary, except where the failure to be so qualified would not have a Material Adverse Effect, and (c) has all requisite corporate power and authority to own or lease and operate its assets and carry on its business as presently being conducted.

5.4. Subsidiaries. There are no direct or indirect Subsidiaries of the Company.

5.5. Consents. Except as set forth on Schedule 5.5, neither the execution, delivery or performance of this Agreement or the other Transaction Documents by the Company, nor the consummation by it of the obligations and transactions contemplated hereby or thereby (including, without limitation, the issuance, the reservation for issuance and the delivery of the Securities) requires any consent of, authorization by, exemption from, filing with or notice to any Governmental Entity or any other Person, other than filings required under applicable U.S. federal and state securities laws or filings with applicable Governmental Entities to perfect the security interests created by the Security Agreement.

5.6. Authorization; Enforcement. The Company has all requisite corporate power and has taken all necessary corporate action required for the due authorization, execution, delivery and performance by the Company of this Agreement and the other Transaction Documents and the consummation of the transactions contemplated hereby and thereby (including, without limitation, the issuance of the Securities and the provision to the Purchaser of the rights contemplated by the Transaction Documents) and no action on the part of the stockholders of the Company is required, except for the actions required pursuant to Section 6.11. The execution, delivery and performance by the Company of each of the Transaction Documents and the consummation by the Company of the transactions contemplated hereby and thereby, have been duly authorized by all necessary corporate action on the part of the Company, except for the stockholder approvals required in connection with the matters set forth in Section 6.11. This Agreement has been duly executed and delivered by the Company, and the other Transaction Documents and instruments referred to herein to which it is a party will be duly executed and delivered by the Company, and each such agreement constitutes or will constitute a legal, valid and binding obligation of the Company enforceable against it in accordance with its terms, except to the extent that enforceability may be limited by bankruptcy, insolvency, reorganization, moratorium, fraudulent conveyance, and any other laws of general application affecting enforcement of creditors' rights generally, and as limited by laws relating to the availability of specific performance, injunctive relief, or other equitable remedies.

5.7. Valid Issuance of Securities. The Notes, when issued, sold and delivered in accordance with the terms and for the consideration set forth in this Agreement, at each Closing, will be duly authorized and a sufficient number of authorized but unissued shares of

Common Stock (which may be unissued or issued but held by the Company as treasury shares) will have been, upon obtaining stockholder approval as contemplated by Section 6.11, reserved for issuance upon conversion of the Notes, and upon such conversion in accordance with the terms of this Agreement and the Notes, the Conversion Shares will be duly authorized, validly issued, fully paid and non-assessable, and free from all taxes and Encumbrances, and will not be subject to preemptive rights or other similar rights of stockholders of the Company, except as set forth herein.

5.8. No Conflicts. Except as set forth on Schedule 5.8 or as specifically contemplated herein, the execution, delivery and performance of each of the Transaction Documents and the consummation of the transactions contemplated hereby and thereby (including, without limitation, the issuance and reservation for issuance, as applicable, of the Securities) will not (a) result in a violation of the certificate of incorporation, as amended, and the by-laws of the Company (the "***Charter Documents***"), (b) conflict with or result in the breach of the terms, conditions or provisions of or constitute a default (or an event which with notice or lapse of time or both would become a default) under, or give rise to any right of termination, acceleration or cancellation under, any material agreement, lease, mortgage, license, indenture, instrument or other contract to which the Company is a party, (c) result in a violation of any law, rule, regulation, order, judgment or decree (including, without limitation, U.S. federal and state securities laws and regulations) applicable to the Company or by which any property or asset of the Company is bound or affected, (d) result in a material violation of any rule or regulation of FINRA or its Trading Markets, or (e) result in the creation of any Encumbrance upon any of the Company's assets. Except as set forth on Schedule 5.8, the Company is not in violation of its Charter Documents, and the Company is not in default (and no event has occurred which, with notice or lapse of time or both, would cause the Company to be in default) under, nor has there occurred any event giving others (with notice or lapse of time or both) any rights of termination, amendment, acceleration or cancellation of, any material agreement, indenture or instrument to which the Company is a party. The business of the Company is not being conducted in violation of any law, ordinance or regulation of any Governmental Entity, except where the violation would not result in a Material Adverse Effect.

5.9. Material Contracts. Each Material Contract is the legal, valid and binding obligation of the Company, enforceable against the Company in accordance with its terms, except to the extent that enforceability may be limited by bankruptcy, insolvency, reorganization, moratorium, fraudulent conveyance, and any other laws of general application affecting enforcement of creditors' rights generally, and as limited by laws relating to the availability of specific performance, injunctive relief, or other equitable remedies. Except as set forth on Schedule 5.9, the Company is in compliance with all material terms of the Material Contracts, and there has not occurred any breach, violation or default or any event that, with the lapse of time, the giving of notice or the election of any Person, or any combination thereof, would constitute a breach, violation or default by the Company under any such Material Contract or, to the knowledge of the Company, by any other Person to any such contract except where such breach, violation or default would not have a Material Adverse Effect. To the knowledge of the Company, it has not been notified that any party to any Material Contract intends to cancel, terminate, not renew or exercise an option under any Material Contract, whether in connection with the transactions contemplated hereby or otherwise.

5.10. Right of First Refusal; Stockholders Agreement; Voting and Registration Rights. Except as provided in this Agreement or the other Transaction Documents, or as otherwise set forth in Schedule 5.10, no party has any right of first refusal, right of first offer, right of co-sale, preemptive right or other similar right or any registration right regarding the securities of the Company. Except pursuant to any agreement listed on Schedule 5.10, there are no provisions of the Charter Documents, and no Material Contracts, other than this Agreement or the other Transaction Documents, which (a) may affect or restrict the voting rights of the Purchaser with respect to the Securities in its capacity as a stockholder of the Company, (b) restrict the ability of the Purchaser, or any successor thereto or assignee or transferee thereof, to transfer the Securities, (c) would adversely affect the Company's or the Purchaser's right or ability to consummate the transactions contemplated by this Agreement or comply with the terms of the other Transaction Documents and the transactions contemplated hereby or thereby, (d) require the vote of more than a majority of the Company's issued and outstanding Common Stock, voting together as a single class, to take or prevent any corporate action, other than those matters requiring a different vote under Delaware law, or (e) entitle any party to nominate or elect any director of the Company or require any of the Company's stockholders to vote for any such nominee or other person as a director of the Company in each case.

5.11. Previous Issuances. All shares of capital stock and other securities previously issued by the Company have been issued in transactions registered under or exempt from the registration requirements under the Securities Act and all applicable state securities or "blue sky" laws, and in compliance with all applicable corporate laws. The Company has not violated the Securities Act or any applicable state securities or "blue sky" laws in connection with the previous issuance of any shares of capital stock or other securities.

5.12. No Integrated Offering. Neither the Company, nor any of its Affiliates or any other Person acting on the Company's behalf, has directly or indirectly engaged in any form of general solicitation or general advertising with respect to the Securities, nor have any of such Persons made any offers or sales of any security of the Company or its Affiliates or solicited any offers to buy any security of the Company or its Affiliates under circumstances that would require registration of the Securities under the Securities Act or any other securities laws or cause this offering of Securities to be integrated with any prior offering of securities of the Company for purposes of the Securities Act or any applicable stockholder approval provisions of any Trading Market on which any securities of the Company are listed or designated.

5.13. Financial Statements.

(a) Except as set forth in Schedule 5.13, the Company has filed all reports, schedules, forms, statements and other documents required to be filed by the Company under the Securities Act and the Exchange Act, including pursuant to Section 13(a) or 15(d) thereof, since January 1, 2010 (the foregoing materials, including the exhibits thereto and documents incorporated by reference therein, being collectively referred to herein as the "***SEC Reports***") on a timely basis or has received a valid extension of such time of filing and has filed any such SEC Reports prior to the expiration of any such extension. As of their respective dates, the SEC Reports complied as to form in all material respects with the requirements of the Securities Act and the Exchange Act, as applicable, and none of the SEC Reports, when filed, contained any

untrue statement of a material fact or omitted to state a material fact required to be stated therein or necessary in order to make the statements therein, in the light of the circumstances under which they were made, not misleading. All agreements to which the Company is a party or to which the property or assets of the Company are subject, which are required to be described in or filed as exhibits to an SEC Report, have been so described or filed.

(b) The financial statements of the Company included in the SEC Reports comply in all material respects with applicable accounting requirements and the rules and regulations of the Commission with respect thereto as in effect at the time of filing. Such financial statements have been prepared in accordance with GAAP, except as may be otherwise specified in such financial statements or the notes thereto and except that unaudited financial statements may not contain all footnotes required by GAAP, and fairly present the financial position of the Company as of and for the dates thereof and the results of operations and cash flows for the periods then ended, subject, in the case of unaudited statements, to normal, immaterial, year-end audit adjustments.

5.14. No Undisclosed Material Liabilities. There are no liabilities of the Company of any kind whatsoever, whether interest-bearing indebtedness, or liabilities accrued, contingent, absolute, determined, determinable or otherwise, other than liabilities:

(a) reflected in the financial statements (including the footnotes thereto) included in the SEC Reports;

(b) disclosed on Schedule 5.14 hereto; or

(c) created under, or incurred in connection with, this Agreement or the other Transaction Documents.

5.15. Absence of Litigation. There is no claim, action, suit, arbitration, investigation or other proceeding pending against, or to the knowledge of the Company, threatened against or affecting, the Company or any of its properties or, to the knowledge of the Company, any of its respective officers or directors before any Governmental Entity, except as disclosed on Schedule 5.15 hereto.

5.16. Taxes. Except as set forth on Schedule 5.16, the Company has properly filed all federal, foreign, state, local, and other tax returns and reports which are required to be filed by it, which returns and reports were properly completed and are true and correct in all material respects, and all taxes, interest, and penalties due and owing have been timely paid. There are no outstanding waivers or extensions of time with respect to the assessment or audit of any tax or tax return of the Company, or claims now pending or matters under discussion between the Company and any taxing authority in respect of any tax of the Company. The Company has no material uncertain tax positions pursuant to FASB Interpretation 48 (FIN 48), *Accounting for Uncertainty in Income Taxes*.

5.17. Employee Matters.

(a) The Company has listed any "employee benefit plan" subject to the Employee Retirement Income Security Act of 1974, as amended ("***ERISA***"), that it maintains for employees on Schedule 5.17(a).

(b) Except as set forth on Schedule 5.17(b), (i) no director or officer or other employee of the Company will become entitled to any retirement, severance, change of control, or similar benefit or enhanced or accelerated benefit (including any acceleration of vesting) or lapse of repurchase rights or obligations with respect to any employee benefit plan subject to ERISA or other benefit under any compensation plan or arrangement of the Company (each, an "***Employee Benefit Plan***") as a result of the transactions contemplated in this Agreement; and (ii) no payment made or to be made to any current or former employee or director of the Company, by reason of the transactions contemplated hereby (whether alone or in connection with any other event, including, but not limited to, the consummation of a change of control or a termination of employment) will constitute an "excess parachute payment" within the meaning of Section 280G of the Code.

(c) No executive officer, to the knowledge of the Company, is, or is now reasonably expected to be, in violation of any term of any employment contract, confidentiality, disclosure or proprietary information agreement or non-competition agreement, or any other contract or agreement or any restrictive covenant with the Company, and, to the knowledge of the Company, the continued employment of each such executive officer does not subject the Company to any material liability with respect to any of the foregoing matters.

(d) The Company is in compliance with all applicable federal, state, local and foreign statutes, laws (including, without limitation, common law), judicial decisions, regulations, ordinances, rules, judgments, orders and codes respecting employment, employment practices, labor, terms and conditions of employment and wages and hours, except where the failure to comply would not have a Material Adverse Effect, and no work stoppage or labor strike against the Company is pending or, to its knowledge, threatened, nor is the Company involved in or, to its knowledge, threatened with any labor dispute, grievance or litigation relating to labor matters involving any current or former employees of the Company or independent contractors. There are no suits, actions, disputes, claims (other than routine claims for benefits), investigations or audits pending or, to the knowledge of the Company, threatened in connection with any Employee Benefit Plan, but excluding any of the foregoing which would not have a Material Adverse Effect. Each Employee Benefit Plan subject to the Patient Protection and Affordable Care Act, as modified by the Health Care and Education Reconciliation Act, and related regulations, has been operated in compliance therewith and is a "grandfathered health plan" as defined therein.

(e) Except as set forth on Schedule 5.17(e), no Key Employee of the Company has advised the Company (orally or in writing) that he or she intends to

terminate employment with the Company, nor does the Company have a present intention to terminate the employment of any officer or Key Employee.

5.18. Compliance with Laws.

(a) The Company has been and is in material compliance with the terms of, all franchises, permits, licenses and other rights and privileges necessary to conduct the Company's present and proposed business and is in compliance with and has not violated, in any material respect, (i) any judgments, orders, decrees, injunctions or writs applicable to the Company, or (ii) any applicable provisions of any laws, statutes, ordinances, rules or regulations applicable to the conduct of the Company's business, including the ownership, testing, development, manufacture, packaging, processing, use, distribution, marketing, labeling, promotion, sale, offer for sale, storage, import, export or disposal of any drug or drug candidate under development, manufactured or distributed by the Company (collectively, "***Applicable Laws***").

(b) Except as set forth on Schedule 5.18, each of the Company and its subsidiaries:

(i) has not received any FDA Form 483, notice of adverse finding, warning letter, untitled letter or other correspondence or notice from the U.S. Food and Drug Administration (the "***FDA***") or any other federal, state, local or foreign governmental or regulatory authority alleging or asserting material noncompliance with any Applicable Laws or any licenses, certificates, approvals, clearances, authorizations, permits and supplements or amendments thereto required by any such Applicable Laws ("***Authorizations***");

(ii) possesses all material Authorizations and such Authorizations are valid and in full force and effect and the Company is not in material violation of any term of any such Authorizations;

(iii) has not received notice of any claim, action, suit, proceeding, hearing, enforcement, investigation, arbitration or other action from the FDA or any other federal, state, local or foreign governmental or regulatory authority or third party alleging that any product operation or activity is in material violation of any Applicable Laws or Authorizations and has no knowledge that the FDA or any other federal, state, local or foreign governmental or regulatory authority or third party is considering any such claim, litigation, arbitration, action, suit, investigation or proceeding;

(iv) has not received notice that the FDA or any other federal, state, local or foreign governmental or regulatory authority has taken, is taking or intends to take action to limit, suspend, modify or revoke any material Authorizations and has no knowledge that the FDA or

any other federal, state, local or foreign governmental or regulatory authority is considering such action;

(v) has filed, obtained, maintained or submitted all material reports, documents, forms, notices, applications, records, claims, submissions and supplements or amendments as required by any Applicable Laws or Authorizations and that all such reports, documents, forms, notices, applications, records, claims, submissions and supplements or amendments were materially complete and correct on the date filed (or were corrected or supplemented by a subsequent submission); and

(vi) has not, either voluntarily or involuntarily, initiated, conducted, or issued or caused to be initiated, conducted or issued, any recall, market withdrawal or replacement, safety alert, "dear doctor" letter, or other notice or action relating to the alleged lack of safety or efficacy of any product or any alleged product defect or violation and, to the Company's knowledge, no third party has initiated, conducted or intends to initiate any such notice or action.

(c) The studies, tests and preclinical and clinical trials conducted by or on behalf of the Company or any of its subsidiaries were and, if still pending, are being conducted in accordance with experimental protocols, procedures and controls pursuant to accepted professional scientific standards and all Applicable Laws and Authorizations, including, without limitation, the Federal Food, Drug and Cosmetic Act and the rules and regulations promulgated thereunder (collectively, "***FFDCA***"); the descriptions of the results of such studies, tests and trials contained in the SEC Reports are accurate and complete and fairly present the data derived from such studies, tests and trials; the Company is not aware of any studies, tests or trials, the results of which the Company believes reasonably call into question the study, test, or trial results described or referred to in the SEC Reports when viewed in the context in which such results are described and the clinical state of development; and, since January 1, 2008, the Company has not received any notices or correspondence from the FDA or any other federal, state, local or foreign governmental or regulatory authority requiring the termination, suspension or material modification of any studies, tests or preclinical or clinical trials conducted by or on behalf of the Company.

5.19. Brokers. There is no investment banker, broker, finder, financial advisor or other Person which has been retained by or is authorized to act on behalf of the Company who might be entitled to any fee or commission in connection with the transactions contemplated by this Agreement.

5.20. Environmental Matters.

(a) (i) (i) No written notice, notification, demand, request for information, citation, summons, complaint or order has been received by, and no investigation, action, claim, suit, proceeding or review is pending or, to the knowledge of

the Company, threatened by any Person against the Company and no penalty has been assessed against the Company with respect to any matters relating to or arising out of any Environmental Law; (ii) the Company is in compliance with all Environmental Laws except where the failure to comply would not have a Material Adverse Effect; and (iii) to the knowledge of the Company there are no liabilities of or relating to the Company relating to or arising out of any Environmental Law except such as would not have a Material Adverse Effect, and, to the knowledge of the Company, there is no existing condition, situation or set of circumstances which could reasonably be expected to result in such a liability.

(b) For purposes of this Agreement, the term "***Environmental Laws***" means federal, state, local and foreign statutes, laws, judicial decisions, regulations, ordinances, rules, judgments, orders, codes, injunctions, permits and governmental agreements relating to human health and the environment, including, but not limited to, Hazardous Materials; and the term "***Hazardous Material***" means all substances or materials regulated as hazardous, toxic, explosive, dangerous, flammable or radioactive under any Environmental Law including, but not limited to: (i) petroleum, asbestos, or polychlorinated biphenyls and (ii) in the United States, all substances defined as Hazardous Substances, Oils, Pollutants or Contaminants in the National Oil and Hazardous Substances Pollution Contingency Plan.

5.21. Intellectual Property Matters.

(a) "***Intellectual Property***" means any and all of the following arising under the laws of the United States, any other jurisdiction or any treaty regime: (i) all inventions (whether patentable or unpatentable and whether or not reduced to practice), all improvements thereon, and all patents, patent applications and patent disclosures, together with all reissuances, continuations, continuations-in-part, revisions, extensions and reexaminations thereof, (ii) all trademarks, service marks, trade dress, logos, trade names and corporate names, together with all translations, adaptations, derivations and combinations thereof and including all goodwill associated therewith, and all applications, registrations and renewals in connection therewith, (iii) all copyrightable works, all copyrights and all applications, registrations and renewals in connection therewith, (iv) all trade secrets and confidential business information (including, without limitation, ideas, research and development, know-how, formulas, compositions, manufacturing and production processes and techniques, technical data, designs, drawings, specifications, customer and supplier lists, pricing and cost information and business and marketing plans and proposals), (v) all computer software (including, without limitation, data and related documentation and except for any commercial "shrink-wrapped" software) and source codes (other than open source codes), (vi) all other proprietary rights, (vii) all copies and tangible embodiments of the foregoing (in whatever form or medium) and (viii) all licenses or agreements in connection with the foregoing. "***Company Intellectual Property***" means all Intellectual Property which is used in connection with, and is material to, the business of the Company and all Intellectual Property owned by the Company, provided that any Intellectual Property that is licensed by the Company shall be included within the meaning of Company

Intellectual Property only within the scope of use by the Company or in connection with the Company's business.

(b) Except as set forth on Schedule 5.21(b), with respect to each item of Company Intellectual Property that is material to the Company's business:

(i) The Company possesses all rights, titles and interests in and to the item if owned by the Company, as applicable, free and clear of any Encumbrance, license or other restriction, and possesses all rights necessary in the case of a licensed item to use such item in the manner in which it presently uses the item or reasonably contemplates using such item, and the Company has taken or caused to be taken reasonable and prudent steps to protect its rights in and to, and the validity and enforceability of, the item owned by the Company;

(ii) the item if owned by the Company is not, and if licensed, to the knowledge of the Company is not, subject to any outstanding injunction, judgment, order, decree, ruling or charge naming the Company;

(iii) no action, suit, proceeding, hearing, investigation, charge, complaint, claim or demand is pending or, to the knowledge of the Company, has been or is being threatened which challenges the legality, validity, enforceability, use or ownership of the item;

(iv) to the knowledge of the Company, the item if owned by the Company does not infringe upon any valid and enforceable Intellectual Property right or other right of any third party;

(v) to the knowledge of the Company, no third party has infringed upon or misappropriated the Company's intellectual property rights in the item;

(vi) the Company is not party to any option, license, sublicense or agreement of any kind covering the item that it is in breach or default thereunder, and to the knowledge of the Company and no event has occurred which, with notice or lapse of time, would constitute such a breach or default or permit termination, modification or acceleration thereunder; and

(vii) each option, license, sublicense or agreement of any kind covering the item is legal, valid, binding, enforceable and in full force and effect.

The Company has provided to the Purchaser a list of all patents, copyrights, trademarks and services marks of the Company included in the Company Intellectual Property that are registered with or issued by or pending before the U.S. or

any foreign patent, trademark or copyright office as of the date of the Initial Closing (the "***IP Summary***"). All registered patents, copyrights, trademarks and service marks included on the IP Summary (x) if owned by the Company and (y) if licensed, to the knowledge of the Company, are valid and subsisting and are not subject to any claims, Encumbrances, taxes or other fees except for periodic filing, annuity and maintenance fees and Permitted Liens. Except as set forth on the IP Summary, the Company has not infringed upon or misappropriated any valid and enforceable Intellectual Property rights of third parties, and there is no pending or, to the knowledge of the Company, threatened claim or litigation against the Company contesting the right to use any third party's Intellectual Property rights, asserting the misuse of any thereof, or asserting the infringement or other violation thereof.

(c) None of the Key Employees of the Company are obligated under any contract (including, without limitation, licenses, covenants, or commitments of any nature) or other agreement, or subject to any judgment, decree, or order of any court or administrative agency, that would interfere with the use of his or her reasonable diligence to promote the interests of the Company or that would conflict with the Company's business as presently conducted. Neither the execution, delivery or performance of this Agreement, nor the carrying on of the Company's business by the employees of the Company, nor the conduct of the Company's businesses as presently conducted, will violate or result in a breach of the terms, conditions or provisions of, or constitute a default under, any contract, covenant, or instrument under which any such Key Employee is obligated, and which violation, breach or default would be materially adverse to the Company.

(d) The Company has entered into confidentiality and proprietary information and assignment of inventions agreements, substantially in the form previously provided to the Purchaser, with the executive officers of the Company. The Company is not aware of any violation by any such executive officers of such agreements.

(e) No stockholder, member, director, officer or employee of the Company has any interest, right, title or interest in any of the Company Intellectual Property.

(f) To the knowledge of the Company, it is not, nor will it be, necessary to utilize any inventions, trade secrets or proprietary information of any of its employees made prior to their employment by the Company, except for valid and enforceable inventions, trade secrets or proprietary information that have been assigned to the Company.

(g) The Company maintains policies and procedures regarding data security, privacy and data use that are commercially reasonable and, in any event, comply with the Company's obligations to its customers and applicable laws, rules and regulations. To the knowledge of the Company, there have not been, and the transaction contemplated under this Agreement will not result in, any security breaches of any

security policy, data use restriction or privacy breach under any such policies or any applicable laws, rules or regulations.

5.22. Related-Party Transactions. Except as disclosed in the SEC Reports or as contemplated hereby, no stockholder who is known by the Company to beneficially own 5% or more (on a fully-diluted basis) of any class of equity securities, and no officer or director of the Company or member of his or her immediate family is currently indebted to the Company, nor is the Company indebted (or committed to make loans or extend or guarantee credit) to any of such individuals. Except as set forth in the SEC Reports, as of the date hereof, no stockholder known by the Company to beneficially own 5% or more (on a fully-diluted basis) of any class of equity securities, officer or director of the Company and no member of the immediate family of any stockholder known by the Company to beneficially owns 5% or more (on a fully-diluted basis) of any class of equity securities, officer or director of the Company, is a party to any contract with the Company.

5.23. Title to Property and Assets. The Company does not own any real property. Except as set forth on Schedule 5.23 hereto, the Company owns or has legally enforceable rights to use or hold for use its personal property and assets free and clear of all Encumbrances except Permitted Liens and such other Encumbrances, if any, that individually or in the aggregate, do not and would not detract from the value of any asset or property of the Company or interfere with the use or contemplated use of any personal property of the Company. With respect to any real property, the Company is not in violation in any material respect of any of its leases. All machinery, equipment, furniture, fixtures and other personal property that is material to the Company's business and all buildings, structures and other facilities, if any, including, without limitation, office or other space used by the Company in the conduct of its business and material to its business, are in good operating condition and fit for operation in the ordinary course of business (subject to normal wear and tear) except for any defects which will not interfere with the conduct of normal operations of the Company. The Company has delivered to the Purchaser true and complete copies of any leases related to the real property used by the Company in the conduct of its business.

5.24. Disclosure. The Company understands and confirms that the Purchaser will rely on the foregoing representations in effecting transactions in securities of the Company. No representation or warranty by the Company contained in this Agreement contains any untrue statement of a material fact or omits to state any material fact necessary in order to make the statements made therein, in light of the circumstances under which they were made, not misleading. The Company acknowledges and agrees that the Purchaser does not make and has not made any representations or warranties with respect to the transactions contemplated hereby other than those specifically set forth in Section 4 hereof.

5.25. Absence of Changes. Since the date of the latest audited financial statements included in the SEC Reports, except as set forth in Schedule 5.25 or as contemplated by, or in connection with, this Agreement or the other Transaction Documents, there has not been:

(a) any declaration, setting aside or payment of any dividend or other distribution with respect to any shares of capital stock of the Company or any repurchase,

redemption or other acquisition by the Company of any outstanding shares of its capital stock of the Company;

(b) any amendment of any term of any outstanding security of the Company;

(c) any transaction or commitment made, or any contract, agreement or settlement entered into, by (or judgment, order or decree affecting) the Company relating to its assets or business (including the acquisition or disposition of any material amount of assets) or any relinquishment by the Company of any contract or other right, other than transactions, commitments, contracts, agreements or settlements (excluding settlements of litigation and tax proceedings) in the ordinary course of business;

(d) any (A) grant of any severance or termination pay to (or amendment to any such existing arrangement with) any director, officer or employee of the Company, (B) entering into of any employment, deferred compensation, supplemental retirement or other similar agreement (or any amendment to any such existing agreement) with any director, officer or employee of the Company, (C) increase in, or accelerated vesting and/or payment of, benefits under any existing severance or termination pay policies or employment agreements or (D) increase in or enhancement of any rights or features related to compensation, bonus or other benefits payable to directors, officers or senior employees of the Company other than in the ordinary course of business consistent with past practice; or

(e) any material tax election made or changed, any audit settled or any amended tax returns filed;

(f) any Material Adverse Effect or any event or events that individually or in the aggregate would have a Material Adverse Effect;

(g) any damage, destruction or loss (whether or not covered by insurance) materially and adversely affecting the Company's properties or assets;

(h) any sale, assignment or transfer, or any agreement to sell, assign or transfer, any material asset, liability, property, obligation or right of the Company to any Person, including, without limitation, each Purchaser and its Affiliates, in each case, other than in the ordinary course of business;

(i) any obligation or liability incurred, or any loans or advances made, by the Company to any of its Affiliates, other than expenses allowable in the ordinary course of business of the Company;

(j) any purchase or acquisition of, or agreement, plan or arrangement to purchase or acquire, any material property, rights or assets other than in the ordinary course of business of the Company;

(k) any assignment, lease or other transfer or disposition, or any other agreement or arrangement therefor by the Company of any property or equipment having a value in excess of $50,000 except in the ordinary course of business;

(l) any waiver of any rights or claims of the Company, except for such waivers which would not have a Material Adverse Effect;

(m) any agreement or commitment by the Company to do any of the foregoing or any material transaction by the Company outside the ordinary course of business of the Company;

(n) any lien upon, or adversely affecting, any property or other assets of the Company, except for such liens which would not have a Material Adverse Effect; or

(o) a determination by either the Company or the Commission that the Company is a "shell company" or a "blank check company," each as defined by the applicable rules and regulations of the Commission.

5.26. Illegal Payments. Neither the Company, nor, to the best knowledge of the Company, any director, officer, agent or employee of the Company has paid, caused to be paid, or agreed to pay, directly or indirectly, in connection with the business of the Company: (a) to any government or agency thereof, any agent or any supplier or customer, any bribe, kickback or other similar payment; (b) any contribution to any political party or candidate (other than from personal funds of directors, officers or employees not reimbursed by their respective employers or as otherwise permitted by applicable law); or (c) intentionally established or maintained any unrecorded fund or asset or made any false entries on any books or records for any purpose.

5.27. Suppliers and Customers. The Company does not have any knowledge of any termination, cancellation or threatened termination or cancellation or limitation of, or any material dissatisfaction with, the business relationship between the Company and any material supplier, customer, vendor, customer or client.

5.28. Regulatory Permits. The Company possesses all material certificates, authorizations and permits issued by the appropriate federal, state, local or foreign regulatory authorities necessary to conduct its business, as they are currently being conducted ("***Material Permits***"), and the Company has not received any notice of proceedings relating to the revocation or modification of any Material Permit.

5.29. Insurance. The Company maintains the insurance policies set forth on Schedule 5.29. The Company carries directors and officers insurance coverage in the amount set forth on Schedule 5.29. The Company has no reason to believe that it will not be able to renew its existing insurance coverage as and when such coverage expires or to obtain similar coverage from similar insurers as may be necessary to continue its business without a significant increase in cost.

5.30. Indebtedness. Except as disclosed in Schedule 5.30 and other than Permitted Indebtedness, the Company (i) has no outstanding Indebtedness, (ii) is not a party to

any contract, agreement or instrument, the violation of which, or default under which, by any other party to such contract, agreement or instrument could reasonably be expected to result in a Material Adverse Effect, (iii) is not in violation of any term of or in default under any contract, agreement or instrument relating to any Indebtedness, except where such violations and defaults would not result, individually or in the aggregate, in a Material Adverse Effect, or (iv) is not a party to any contract, agreement or instrument relating to any Indebtedness, the performance of which, in the judgment of the Company's officers, has or is expected to have a Material Adverse Effect. Schedule 5.30 provides a detailed description of the material terms of any such outstanding Indebtedness.

5.31. Ranking of the Notes. No Indebtedness of the Company is senior to or ranks *pari passu* with the Notes in right of payment, whether with respect of payment of redemptions, interest, damages or upon liquidation or dissolution or otherwise.

5.32. Investment Company. The Company is not, and is not an Affiliate of, and immediately after receipt of payment for the Securities, will not be or be an Affiliate of, an "investment company" within the meaning of the Investment Company Act of 1940, as amended.

5.33. Securities and Exchange Act Requirements. The Company is required to file periodic and other reports with the Commission pursuant to Section 12(g) of the Exchange Act, and the Company has filed all such required reports with the Commission.

5.34. Accountants. Odenberg, Ullakko, Muranishi & Co. LLP ("***OUM***"), who expressed their opinion with respect to the financial statements included in the SEC Reports, are independent accountants as required by the Securities Act and the rules and regulations promulgated thereunder. There are no disagreements of any kind presently existing, or reasonably anticipated by the Company to arise, between the Company and OUM, and except as set forth on Schedule 5.34, upon completion of the Initial Closing, the Company will be current with respect to any fees owed to such accounting firm.

5.35. Application of Takeover Protections; Exemption under Section 16. The Company and its Board of Directors have taken all necessary action, if any, in order to (a) render inapplicable any control share acquisition, business combination, poison pill (including any distribution under a rights agreement) or other similar anti-takeover provision under the Company's Charter Documents or the laws of its state of incorporation (including Section 203 of the Delaware General Corporation Law) that is or could become applicable to each Purchaser as a result of such Purchaser and the Company fulfilling their obligations or exercising their rights under the Transaction Documents, including without limitation as a result of the Company's issuance of the Securities and such Purchaser's ownership of the Securities, and (b) exempt the acquisition of the Securities by the Purchaser, to the extent applicable, under Rule 16b-3 promulgated under the Act.

5.36. Stock Options. With respect to stock options issued pursuant to the Company's Employee Benefit Plans (i) except as set forth on Schedule 5.36 hereto, each grant of a stock option was duly authorized no later than the date on which the grant of such stock option was by its terms to be effective by all necessary corporate action, including, as applicable,

approval by the Board of Directors (or a duly constituted and authorized committee thereof) and any required stockholder approval by the necessary number of votes or written consents and (ii) each such grant was made in accordance with the material terms of the Employee Benefit Plans, the Securities Act and all other applicable laws and regulatory rules or requirements.

6. Covenants.

6.1. Best Efforts. Each party shall use its best efforts timely to satisfy each of the conditions to be satisfied by it as provided in Section 7 of this Agreement.

6.2. Form D and Blue Sky. The Company agrees to file a Form D with respect to the Securities as required under Regulation D and to provide a copy thereof to the Purchasers promptly after such filing. The Company shall, on or before each Closing Date, take such action as the Company shall reasonably determine is necessary in order to obtain an exemption for or to qualify the Securities for sale to the Purchasers at the Closing pursuant to this Agreement under applicable securities or "blue sky" laws of the states of the United States (or to obtain an exemption from such qualification), and shall provide evidence of any such action so taken to the Purchasers on or prior to the Closing Date. The Company shall make all filings and reports relating to the offer and sale of the Securities, and the resale of the Securities, as may be required under applicable securities or "blue sky" laws of the states of the United States following the Closing Date.

6.3. Reporting Status. Until the date on which the Purchasers shall have sold all the Conversion Shares and none of the Notes are outstanding (the "***Reporting Period***"), the Company shall (i) timely file all reports required to be filed with the Commission pursuant to the Exchange Act or the rules and regulations thereunder and (ii) not take any action or file any document (whether or not permitted by the Securities Act or the rules promulgated thereunder) to terminate or suspend the Company's reporting and filing obligations under the Exchange Act or Securities Act.

6.4. Use of Proceeds. The Company will use the proceeds from the sale of the Securities for general corporate purposes, including sales, marketing, working capital, general and administrative expenses and not for (i) the repayment of any outstanding Indebtedness of the Company or (ii) the redemption or repurchase of any of its equity securities.

6.5. Financial Information. As long as any Notes are outstanding, the Company agrees to send the following to the Purchasers during the Reporting Period (i) unless the following are filed with the Commission through EDGAR and are available to the public through the EDGAR system, within one (1) Business Day after the filing thereof with the Commission, a copy of its Annual Reports and Quarterly Reports on Form 10-K, 10-KSB, 10-Q or 10-QSB, any interim reports or any consolidated balance sheets, income statements, stockholders' equity statements and/or cash flow statements for any period other than annual, any Current Reports on Form 8-K and any registration statements (other than on Form S-8) or amendments filed pursuant to the Securities Act, (ii) on the same day as the release thereof, facsimile or e-mailed copies of all press releases issued by the Company, and (iii) copies of any notices and other information made available or given to the stockholders of the Company generally, contemporaneously with the making available or giving thereof to the stockholders.

As used herein, "***Business Day***" means any day other than Saturday, Sunday or other day on which commercial banks in The City of New York are authorized or required by law to remain closed.

6.6. Listing. The Company shall promptly secure the listing of all of the Registrable Securities upon each national securities exchange and automated quotation system, if any, upon which the Common Stock is then listed (subject to official notice of issuance) and shall maintain, in accordance with the Notes, such listing of all Registrable Securities from time to time issuable under the terms of the Transaction Documents. The Company shall pay all fees and expenses in connection with satisfying its obligations under this Section 6.6.

6.7. Fees. Upon consummation of each Closing pursuant to this Agreement or in the event that the Company elects to terminate this Agreement, the Company shall pay, reimburse and hold the Purchasers harmless from liability for the payment of all reasonable fees and expenses incurred by them in connection with the preparation and negotiation of the Transaction Documents and the consummation of the transactions contemplated hereby. The reasonable fees and expenses of the Purchasers may include, without limitation, the reasonable fees and expenses of counsel and out of pocket expenses, including diligence and travel expenses, of the Purchasers arising in connection with the preparation, negotiation and execution of the Transaction Documents and the consummation of the transactions contemplated thereby.

6.8. Pledge of Securities. The Company acknowledges and agrees that the Securities may be pledged by the Purchasers in connection with a bona fide margin agreement or other loan or financing arrangement that is secured by the Securities. The pledge of Securities shall not be deemed to be a transfer, sale or assignment of the Securities hereunder, and in effecting a pledge of Securities the Purchasers shall not be required to provide the Company with any notice thereof or otherwise make any delivery to the Company pursuant to this Agreement or any other Transaction Document. The Company hereby agrees to execute and deliver such documentation as a pledgee of the Securities may reasonably request in connection with a pledge of the Securities to such pledgee by the Purchasers.

6.9. Disclosure of Transactions and Other Material Information. On or before 8:30 a.m., New York City time, on the second Business Day following the date of this Agreement, the Company shall issue a press release and file a Current Report on Form 8-K describing the terms of the transactions contemplated by the Transaction Documents in the form required by the Exchange Act and attaching the material Transaction Documents (including, without limitation, this Agreement (and all schedules to this Agreement) and the form of the Notes) as exhibits to such filing (including all attachments, the "8-K Filing"). Subject to the foregoing, neither the Company nor the Purchasers shall issue any press releases or any other public statements with respect to the transactions contemplated hereby; provided, however, that the Company shall be entitled, without the prior approval of the Purchasers, to make any press release or other public disclosure with respect to such transactions (i) in substantial conformity with the 8-K Filing and contemporaneously therewith and (ii) as is required by applicable law and regulations (provided that in the case of clause (i) the Purchasers shall be consulted by the Company in connection with any such press release or other public disclosure prior to its release). Without the prior written consent of a given Purchaser, neither the Company nor any of

its affiliates shall disclose the name of such Purchasers in any filing, announcement, release or otherwise.

6.10. Corporate Existence. So long as any Purchaser beneficially owns any Securities, the Company shall not be party to any Change of Control transaction (as defined in the Notes) unless the Company is in compliance with the applicable provisions governing Change of Control transactions set forth in the Notes.

6.11. Reservation of Shares. The Company shall take all action necessary to, at all times from the Increase Deadline, have authorized and reserved for the purpose of issuance upon conversion of the Notes, no less than the number of shares of Common Stock issuable (i) upon conversion of $4,500,000 aggregate principal amount of the Notes, and (ii) upon conversion of accrued and unpaid PIK Interest potentially issuable under the Notes through the Maturity Date (as defined in the Notes). The "***Increase Deadline***" means the earlier of (a) six months from the Initial Closing Date, and (b) one Business Day after the Company's 2011 annual meeting of stockholders.

6.12. Conduct of Business. The business of the Company shall not be conducted in violation of any law, ordinance or regulation of any governmental entity, except where such violations would not result, either individually or in the aggregate, in a Material Adverse Effect.

6.13. Ranking of the Notes. No Indebtedness of the Company may be incurred that is senior to or ranks *pari passu* with the Notes in right of payment, whether with respect of payment of redemptions, interest, damages or upon liquidation or dissolution or otherwise.

6.14. Follow-on Offering. Within thirty (30) days from the Initial Closing, the Company shall prepare and file a registration statement on Form S-1 registering the offer and sale of up to $20,000,000 of equity securities (including common stock, common stock equivalents and preferred stock), to be offered and sold by the Company on a primary basis (the "***Follow-on Offering***"). The Company shall use commercially reasonable efforts to have the foregoing registration statement declared effective by the staff of the Commission and to complete the Follow-on Offering as promptly as practicable. The failure to timely file a registration statement for the Follow-on Offering within thirty (30) days from the Initial Closing Date shall be deemed a Filing Failure for purposes of Section 11.5 of this Agreement.

7. Conditions of Parties' Obligations.

7.1. Conditions of the Purchasers' Obligations at the Initial Closing and the Subsequent Closings. The obligations of the Purchasers under Section 2 hereof are subject to the fulfillment, prior to each Closing, of all of the following applicable conditions, any of which may be waived in whole or in part by the Purchasers in their absolute discretion.

(a) Representations and Warranties. The representations and warranties of the Company contained in this Agreement and in any certificate, if any, or other writing, if any, delivered by the Company pursuant hereto shall be true and correct (i) on and as of the Initial Closing Date with the same effect as though such representations and warranties had been made on and as of the Initial Closing Date

(except to the extent expressly made as of an earlier date in which case as of such earlier date) and (ii) on and as of each Subsequent Closing Date with the same effect as though such representations and warranties had been made on and as of such Subsequent Closing Date (except to the extent expressly made as of an earlier date in which case as of such earlier date).

(b) Performance. The Company shall have performed and complied in all material respects with all agreements, obligations and conditions contained in this Agreement that are required to be performed or complied by it on or before the applicable Closing.

(c) Qualification Under State Securities Laws. All registrations, qualifications, permits and approvals, if any, required under applicable state securities laws shall have been obtained for the lawful execution, delivery and performance of this Agreement or the other Transaction Documents.

(d) Control Agreement. The Company shall have executed and delivered each Control Agreement on or before the Initial Closing.

(e) Supporting Documents. The Purchasers at each Closing shall have received the following:

(i) An opinion from Latham & Watkins LLP, counsel to the Company, dated as of the date of the applicable Closing, in a form reasonably satisfactory to the Purchasers; and

(ii) Copies of resolutions of the Board of Directors, certified by the Secretary of the Company, authorizing and approving by the disinterested directors the execution, delivery and performance of the Transaction Documents and all other documents and instruments to be delivered pursuant hereto and thereto.

(f) Consents and Waivers. The Company shall have obtained all consents or waivers necessary to execute and perform its obligations under this Agreement and the other Transaction Documents (including consents and waivers listed on Schedule 5.5). All corporate and other action and governmental filings necessary to effectuate the terms of this Agreement, the other Transaction Documents, and other agreements and instruments executed and delivered by the Company in connection herewith shall have been made or taken, and no Material Adverse Effect has occurred with respect to the operation of the Company's business.

(g) No Material Adverse Effect. There shall have been no Material Adverse Effect with respect to the Company since the date of the latest audited balance sheet of the Company included in the SEC Reports.

(h) Fees and Expenses of Purchasers. The Company shall have paid (or the Purchasers shall have made arrangements to deduct from the Notes Purchase Price

or the Total Notes Purchase Price, as applicable), in accordance with Section 6.7, the fees, expenses and disbursements of the Purchasers.

(i) No Default. No Event of Default (as defined in the Notes) shall be continuing as of each Closing, after giving effect to the transactions contemplated to occur on each Closing.

(j) Compliance Certificates. The Company shall have provided to the Purchasers, a Compliance Certificate, executed by the Chief Executive Officer (or acting Chief Executive Officer, if applicable) of the Company, dated as of the Closing, to the effect that the conditions specified in subsections (a) "Representations and Warranties", (b) "Performance", (c) "Qualification Under State Securities Laws", (f) "Consents and Waivers" and (i) "No Default" of this Section 7.1 have been satisfied.

7.2. Conditions of the Company's Obligations. The obligations of the Company under Section 2 hereof are subject to the fulfillment prior to or on each Closing of all of the following conditions, any of which may be waived in whole or in part by the Company.

(a) Covenants; Representations and Warranties. (i) The Purchasers at the Closing shall have performed all of its obligations hereunder required to be performed by it at or prior to the Closing and (ii) the representations and warranties of the Purchasers at the Closing contained in this Agreement shall be true and correct at and as of the Closing as if made at and as of the Closing (except to the extent expressly made as of an earlier date, in which case as of such earlier date).

8. Transfer Restrictions; Restrictive Legend.

8.1. Transfer Restrictions. The Purchasers understand that the Company may, as a condition to the transfer of any of the Securities, require that the request for transfer be accompanied by an opinion of counsel reasonably satisfactory to the Company, to the effect that the proposed transfer does not result in a violation of the Securities Act, unless such transfer is covered by an effective registration statement or by Rule 144 or Rule 144A under the Securities Act; provided, however, that an opinion of counsel shall not be required for a transfer by a Purchaser that is (A) a partnership transferring to its partners or former partners in accordance with partnership interests, (B) a corporation transferring to a wholly owned subsidiary or a parent corporation that owns all of the capital stock of such Purchaser, (C) a limited liability company transferring to its members or former members in accordance with their interest in the limited liability company, (D) an individual transferring to such Purchaser's family member or trust for the benefit of an individual Purchaser, (E) transferring its Securities to any Affiliate of such Purchaser, in the case of an institutional investor, or other Person under common management with such Purchaser, or (F) a transfer that is made pursuant to a bona fide gift to a third party; provided, further, that (i) the transferee in each case agrees to be subject to the restrictions in this Section 8 and provides the Company with a representation letter containing substantially the same representations and warranties set forth in Section 4 hereof, (ii) the Company satisfies itself that the number of transferees is sufficiently limited and (iii) in the case of transferees that are partners or limited liability company members, the transfer is for no consideration. It is understood that the certificates evidencing any Securities may bear substantially the following

legends (in addition to any other legends as legal counsel for the Company deems necessary or advisable under the applicable state and federal securities laws or any other agreement to which the Company is a party):

"THESE SECURITIES HAVE NOT BEEN REGISTERED UNDER THE SECURITIES ACT OF 1933 OR ANY APPLICABLE STATE SECURITIES LAWS. THEY MAY NOT BE SOLD, OFFERED FOR SALE, PLEDGED OR HYPOTHECATED IN THE ABSENCE OF A REGISTRATION STATEMENT IN EFFECT WITH RESPECT TO THE SECURITIES UNDER SUCH ACT OR APPLICABLE STATE SECURITIES LAWS OR AN OPINION OF COUNSEL SATISFACTORY TO THE COMPANY THAT SUCH REGISTRATION IS NOT REQUIRED OR UNLESS SOLD PURSUANT TO RULE 144 OR RULE 144A OF SUCH ACT."

8.2. Unlegended Certificates. The Company shall be obligated to reissue promptly unlegended certificates at the request of any holder thereof if (a) the holder shall have obtained an opinion of counsel reasonably acceptable to the Company to the effect that, or the Company is otherwise satisfied that, the securities proposed to be disposed of may lawfully be so disposed of without registration, qualification or legend, or (b) the securities represented by the certificate containing the foregoing legend have been registered for resale as contemplated in Section 11 of this Agreement, in which case the removal shall be predicated on the undertaking by such Purchaser that the securities will only be sold pursuant to such registration statement(s) or an available exemption from registration.

9. Registration, Transfer and Substitution of Certificates for Shares.

9.1. Stock Register; Ownership of Securities. The Company will keep at its principal office a register in which the Company will provide for the registration of transfers of the Notes. The Company may treat the Person in whose name any of the Notes are registered on such register as the owner thereof and the Company shall not be affected by any notice to the contrary. All references in this Agreement to a "holder" of any Securities shall mean the Person in whose name such Securities are at the time registered on such register.

9.2. Transfer Agent Instruction. Subject to satisfaction of either condition set forth in Section 8.2, the Company shall issue irrevocable instructions to its transfer agent, and any subsequent transfer agent, to credit shares to the applicable balance accounts at The Depository Trust Company ("***DTC***"), registered in the name of the Purchaser or its nominee(s), for the Conversion Shares or upon conversion of the Notes in such amounts as specified from time to time by the Purchaser to the Company upon conversion of the Notes. The Company warrants that no instruction other than the Irrevocable Transfer Agent Instructions referred to in this Section 9.2 will be given by the Company to its transfer agent and that the Securities shall otherwise be freely transferable on the books and records of the Company as and to the extent provided in this Agreement and the other Transaction Documents. If a Purchaser effects a transfer of the Securities in accordance with Section 8.1, the Company shall permit the transfer and shall promptly instruct its transfer agent to issue one or more certificates or credit shares to the applicable balance accounts at DTC in such name and in such denominations as specified by such Purchaser to effect such transfer. In the event that any sale, assignment or transfer involves

Conversion Shares sold, assigned or transferred pursuant to an effective registration statement or pursuant to Rule 144, the transfer agent shall issue such Securities to the Purchaser, assignee or transferee, as the case may be, without any restrictive legend. The Company acknowledges that a breach by it of its obligations hereunder will cause irreparable harm to the Purchasers. Accordingly, the Company acknowledges that the remedy at law for a breach of its obligations under this Section 9.2 will be inadequate and agrees, in the event of a breach or threatened breach by the Company of the provisions of this Section 9.2, that the Purchaser shall be entitled, in addition to all other available remedies, to an order and/or injunction restraining any breach and requiring immediate issuance and transfer, without necessity of showing economic loss and without bond or other security being required.

9.3. Replacement of Certificates. Upon receipt of evidence reasonably satisfactory to the Company of the loss, theft, destruction or mutilation of any certificate representing Notes, and, in the case of any such loss, theft or destruction, upon delivery of an indemnity agreement reasonably satisfactory to the Company or, in the case of any such mutilation, upon surrender of such certificate for cancellation at the office of the Company maintained pursuant to Section 9.1 hereof, the Company at its expense will execute and deliver, in lieu thereof, a new certificate representing Notes of like tenor.

10. Pre-emptive Right of the Purchasers.

10.1. Issuance of Additional Securities. The Company hereby grants to the Purchasers the right to purchase up to 50% (the "***Preemptive Portion***") of any new securities (excluding securities issued in an Exempt Issuance) offered and sold by the Company, ("***New Securities***") at any time after the Initial Closing Date, until $15,000,000 in aggregate New Securities have been offered and sold to any Persons (including the Purchasers). The Preemptive Portion shall be pro rated among the Purchasers with respect to each issuance of New Securities based on each Purchaser's Pro Rata Interest.

10.2. Additional Issuance Notices. The Company shall give written notice (an "***Issuance Notice***") of any proposed issuance or sale of New Securities described in Section 10.1 to the Purchasers within five (5) Business Days following any meeting of the Board of Directors at which such issuance or sale is approved. The Issuance Notice shall, if applicable, be accompanied by a written offer from any prospective purchaser seeking to purchase New Securities and shall set forth the material terms and conditions of the proposed issuance including:

(a) the number and description of the New Securities proposed to be issued and the percentage of the Company's capitalization such issuance would represent;

(b) the proposed issuance date, which shall be at least ten (10) Business Days from the date of the Issuance Notice; and

(c) the proposed purchase price per security and other material terms of the offering.

10.3. Exercise of Pre-Emptive Rights. For a period of five (5) Business Days following the receipt of the Issuance Notice (the "***Exercise Period***"), each Purchaser shall have

the right to elect irrevocably to purchase its Preemptive Portion of the New Securities at the purchase price set forth in the Issuance Notice by delivering a written notice to the Company. The closing of any purchase by such Purchaser shall be consummated concurrently with the consummation of the issuance or sale described in the Issuance Notice. Notwithstanding the foregoing, the closing of any purchase by a Purchaser may be extended beyond the closing of the transaction in the Issuance Notice to the extent necessary to obtain any required third party approvals or consents (and the Company and such Purchaser shall use their respective reasonable efforts to obtain such approvals); *provided*, *however*, any such extension shall not exceed 60 days.

10.4. Sales to Prospective Buyer. If a Purchaser fails to purchase its allotment of the New Securities within the time period described in Section 10.3, the Company shall be free to complete the proposed issuance or sale of New Securities described in the Issuance Notice with respect to which such Purchaser(s) failed to exercise the option set forth in this Section 10 on terms no less favorable to the Company than those set forth in the Issuance Notice (except that the amount of New Securities to be issued or sold by the Company may be reduced); *provided*, that (x) such issuance or sale is closed within thirty (30) Business Days after the expiration of the Exercise Period (subject to the extension of such period for a reasonable time not to exceed 60 days to the extent reasonably necessary to obtain any required third party approvals or consents) and (y) for the avoidance of doubt, the price at which the New Securities are sold is at least equal to or higher than the purchase price described in the Issuance Notice. In the event the Company has not sold such New Securities within such time period, the Company shall not thereafter issue or sell any New Securities without first again offering such securities to the Stockholders in accordance with the procedures set forth in this Section 10.

10.5. Closing of the Issuance. Upon the issuance of any New Securities to the Purchaser in accordance with this Section 10, the Company shall deliver to the Purchaser(s) certificates (if any) evidencing the New Securities, which New Securities shall be issued free and clear of any Encumbrances, and the Company shall so represent and warrant to the Purchaser(s), and further represent and warrant to the Purchaser(s) that such New Securities shall be, upon issuance thereof to the Purchaser(s) and after payment therefor, duly authorized, validly issued, fully paid and non-assessable. The Purchaser(s) shall deliver to the Company the purchase price for the New Securities purchased by it by wire transfer of immediately available funds. Each party to the purchase and sale of New Securities shall take all such other actions as may be reasonably necessary to consummate the purchase and sale including, without limitation, entering into such additional agreements as may be necessary or appropriate.

11. Registration Rights of Purchasers.

11.1. Mandatory Registration. The Company shall prepare, and, as soon as practicable but in no event later than thirty (30) days after the Initial Closing Date (the "***Filing Deadline***"), file with the Commission a Registration Statement on Form S-3 covering the resale of the full amount of the Conversion Shares (including the Conversion Shares underlying the Notes, Additional Notes, as well as Notes that may be issued in payment of PIK Interest) (collectively, the "***Registrable Securities***"). In the event that Form S-3 is unavailable for such a registration, the Company shall use such other form as is available for such a registration on another appropriate form reasonably acceptable to the Purchasers, subject to the provisions of

Section 11.3. The Company shall use its commercially reasonable efforts to have the Registration Statement declared effective by the Commission as soon as practicable, but in no event later than the ***Effectiveness Deadline***, which shall be either (i) 90 days after the Initial Closing Date or (ii) in the event that the Commission reviews the Registration Statement, 120 days after the Initial Closing Date (but in any event, no later than two Business Days from the Commission indicating that it has no further comments on the Registration Statement). By 9:30 am on the Business Day following the Effective Date, the Company shall file with the Commission in accordance with Rule 424 under the Securities Act the final prospectus to be used in connection with sales pursuant to such Registration Statement.

11.2. Legal Counsel. The Purchasers shall have the right to select one legal counsel to review and oversee any registration pursuant to this Section 11, which shall be Ropes & Gray LLP or such other counsel ("***Legal Counsel***") as thereafter designated by the Purchasers. The Company and Legal Counsel shall reasonably cooperate with each other in performing the Company's obligations under this Section 11.

11.3. Ineligibility for Form S-3. In the event that Form S-3 is not available for the registration of the resale of Registrable Securities hereunder, the Company shall (i) register the resale of the Registrable Securities on another appropriate form reasonably acceptable to the Purchasers and (ii) undertake to register the Registrable Securities on Form S-3 as soon as such form is available, provided that the Company shall maintain the effectiveness of the Registration Statement then in effect until such time as a Registration Statement on Form S-3 covering the Registrable Securities has been declared effective by the Commission.

11.4. Sufficient Number of Shares Registered. In the event the number of shares available under a Registration Statement filed pursuant to Section 11.1 is insufficient to cover all of the Registrable Securities required to be covered by such Registration Statement, by virtue of an adjustment of the Conversion Price of the Notes or otherwise, the Company shall amend the applicable Registration Statement, or file a new Registration Statement (on the short form available therefor, if applicable), or both, so as to cover at least the Required Registration Amount as of the trading day immediately preceding the date of the filing of such amendment or new Registration Statement, in each case, as soon as practicable, but in any event not later than fifteen (15) days after the necessity therefor arises. The Company shall use its best efforts to cause such amendment and/or new Registration Statement to become effective as soon as practicable following the filing thereof. For purposes of the foregoing provision, the number of shares available under a Registration Statement shall be deemed "insufficient to cover all of the Registrable Securities" if on any Trading Day after the Filing Date and during the Registration Period (each a "***Test Trading Day***"), the number of shares of Common Stock available for resale under the Registration Statement is less than the Required Registration Amount, determined as of such Test Trading Day, (a) without regard to any limitations on the conversion of the Notes, and (b) assuming that the Notes (including the Additional Notes and any Notes that may be issued in the payment of the PIK Interest), are then convertible into shares of Common Stock at the prevailing Conversion Rate (as defined in the Notes) as of each Test Trading Day.

11.5. Effect of Failure to File and Obtain and Maintain Effectiveness of Registration Statement. If (a) a Registration Statement covering all of the Registrable Securities required to be covered thereby and required to be filed by the Company pursuant to this

Agreement is (i) not filed with the Commission on or before the Filing Deadline (a "***Filing Failure***") or (ii) not declared effective by the Commission on or before the Effectiveness Deadline (an "***Effectiveness Failure***") or (b) on any day after the Effective Date, sales of all of the Registrable Securities required to be included on such Registration Statement cannot be made (other than during an Allowable Grace Period) pursuant to such Registration Statement (including, without limitation, because of a failure to keep such Registration Statement effective, to disclose such information as is necessary for sales to be made pursuant to such Registration Statement or to register a sufficient number of shares of Common Stock) (a "***Maintenance Failure***") then, as partial relief for the damages to any holder by reason of any such delay in or reduction of its ability to sell the underlying shares of Common Stock (which remedy shall not be exclusive of any other remedies available at law or in equity), the Company shall pay to each holder of Registrable Securities relating to such Registration Statement an amount in cash equal to two percent (2.0%) of such holder's Pro Rata Interest in the Total Notes Purchase Price on each of the following dates: (i) the day of a Filing Failure and on every thirtieth day (pro rated for periods totaling less than thirty (30) days) thereafter until such Filing Failure is cured; (ii) the day of an Effectiveness Failure and on every thirtieth day (pro rated for periods totaling less than thirty (30) days) thereafter until such Effectiveness Failure is cured; and (iii) the initial day of a Maintenance Failure and on every thirtieth day (pro rated for periods totaling less than thirty (30) days) thereafter until such Maintenance Failure is cured. The payments to which a holder shall be entitled pursuant to this Section 11.5 are referred to herein as "***Registration Delay Payments***." The first such Registration Delay Payment shall be paid within three (3) Business Days after the event or failure giving rise to such Registration Delay Payment occurred and all other Registration Delay Payments shall be paid on the earlier of (I) the last day of the calendar month during which such Registration Delay Payments are incurred and (II) the third Business Day after the event or failure giving rise to the Registration Delay Payments is cured. In the event the Company fails to make Registration Delay Payments in a timely manner, such Registration Delay Payments shall bear interest at the rate of two percent (2.0%) per month (prorated for partial months) until paid in full.

11.6. Related Obligations. At such time as the Company is obligated to file a Registration Statement with the Commission pursuant to Section 11.1, 11.3 or 11.4, the Company will use its best efforts to effect the registration of the Registrable Securities in accordance with the intended method of disposition thereof and, pursuant thereto, the Company shall have the following obligations:

(a) The Company shall submit to the Commission, within two (2) Business Days after the Company learns that no review of a particular Registration Statement will be made by the staff of the Commission or that the staff has no further comments on a particular Registration Statement, as the case may be, a request for acceleration of effectiveness of such Registration Statement to a time and date not later than two (2) Business Days after the submission of such request. The Company shall keep each Registration Statement effective pursuant to Rule 415 at all times until the earlier of (i) the date as of which the Purchasers may sell all of the Registrable Securities covered by such Registration Statement without restriction pursuant to Rule 144 (or any successor thereto) promulgated under the Securities Act or (ii) the date on which the Purchasers shall have sold all of the Registrable Securities covered by such Registration Statement (the "***Registration Period***"). The Company shall ensure that each Registration

Statement (including any amendments or supplements thereto and prospectuses contained therein) shall not contain any untrue statement of a material fact or omit to state a material fact required to be stated therein, or necessary to make the statements therein (in the case of prospectuses, in the light of the circumstances in which they were made) not misleading.

(b) The Company shall prepare and file with the Commission such amendments (including post-effective amendments) and supplements to a Registration Statement and the prospectus used in connection with such Registration Statement, which prospectus is to be filed pursuant to Rule 424 promulgated under the Securities Act, as may be necessary to keep such Registration Statement effective at all times during the Registration Period, and, during such period, comply with the provisions of the Securities Act with respect to the disposition of all Registrable Securities of the Company covered by such Registration Statement until such time as all of such Registrable Securities shall have been disposed of in accordance with the intended methods of disposition by the seller or sellers thereof as set forth in such Registration Statement. In the case of amendments and supplements to a Registration Statement which are required to be filed pursuant to this Agreement (including pursuant to this Section 11.6(b)) by reason of the Company filing a report on Form 10-Q, Form 10-K or any analogous report under the Exchange Act, the Company shall have incorporated such report by reference into such Registration Statement, if applicable, or shall file such amendments or supplements with the Commission on the same day on which the Exchange Act report is filed which created the requirement for the Company to amend or supplement such Registration Statement.

(c) The Company shall (i) permit Legal Counsel to review and comment upon (A) a Registration Statement at least five (5) Business Days prior to its filing with the Commission and (B) all amendments and supplements to all Registration Statements (except for Annual Reports on Form 10-K, and Quarterly Reports on Form 10-Q and any similar or successor reports) within a reasonable number of days prior to their filing with the Commission, and (ii) not file any Registration Statement or amendment or supplement thereto in a form to which Legal Counsel reasonably objects. The Company shall not submit a request for acceleration of the effectiveness of a Registration Statement or any amendment or supplement thereto without the prior approval of Legal Counsel, which consent shall not be unreasonably withheld. The Company shall furnish to Legal Counsel, without charge, (i) copies of any correspondence from the Commission or the staff of the Commission to the Company or its representatives relating to any Registration Statement, (ii) promptly after the same is prepared and filed with the Commission, one copy of any Registration Statement and any amendment(s) thereto, including financial statements and schedules, all documents incorporated therein by reference, if requested by the Purchasers, and all exhibits and (iii) upon the effectiveness of any Registration Statement, one copy of the prospectus included in such Registration Statement and all amendments and supplements thereto. The Company shall reasonably cooperate with Legal Counsel in performing the Company’s obligations pursuant to this Section 11.

(d) The Company shall furnish to the Purchasers without charge, (i) promptly after the Registration Statement including such Purchaser's Registrable Securities is prepared and filed with the Commission, at least one copy of such Registration Statement and any amendment(s) thereto, including financial statements and schedules, all documents incorporated therein by reference, if requested by the Purchaser, all exhibits and each preliminary prospectus, (ii) upon the effectiveness of any Registration Statement, ten (10) copies of the prospectus included in such Registration Statement and all amendments and supplements thereto (or such other number of copies as the Purchaser may reasonably request) and (iii) such other documents, including copies of any preliminary or final prospectus, as the Purchaser may reasonably request from time to time in order to facilitate the disposition of the Registrable Securities.

(e) The Company shall use its best efforts to (i) register and qualify, unless an exemption from registration and qualification applies, the resale by the Purchaser of the Registrable Securities covered by a Registration Statement under such other securities or "blue sky" laws of all applicable jurisdictions in the United States, (ii) prepare and file in those jurisdictions, such amendments (including post-effective amendments) and supplements to such registrations and qualifications as may be necessary to maintain the effectiveness thereof during the Registration Period, (iii) take such other actions as may be necessary to maintain such registrations and qualifications in effect at all times during the Registration Period, and (iv) take all other actions reasonably necessary or advisable to qualify the Registrable Securities for sale in such jurisdictions; provided, however, that the Company shall not be required in connection therewith or as a condition thereto to (x) qualify to do business in any jurisdiction where it would not otherwise be required to qualify but for this Section 11.6(e), (y) subject itself to general taxation in any such jurisdiction, or (z) file a general consent to service of process in any such jurisdiction. The Company shall promptly notify Legal Counsel and the Purchasers of the receipt by the Company of any notification with respect to the suspension of the registration or qualification of any of the Registrable Securities for sale under the securities or "blue sky" laws of any jurisdiction in the United States or its receipt of notice of the initiation or threatening of any proceeding for such purpose.

(f) The Company shall notify Legal Counsel and the Purchasers in writing of the happening of any event, as promptly as practicable after becoming aware of such event, as a result of which the prospectus included in a Registration Statement, as then in effect, includes an untrue statement of a material fact or omission to state a material fact required to be stated therein or necessary to make the statements therein, in the light of the circumstances under which they were made, not misleading (provided that in no event shall such notice contain any material, nonpublic information), and, promptly prepare a supplement or amendment to such Registration Statement to correct such untrue statement or omission, and deliver ten (10) copies of such supplement or amendment to Legal Counsel and the Purchasers (or such other number of copies as Legal Counsel or the Purchasers may reasonably request). The Company shall also promptly notify Legal Counsel and the Purchasers in writing (i) when a prospectus or any prospectus supplement or post-effective amendment has been filed, and when a Registration Statement or any post-effective amendment has become effective (notification of such effectiveness shall be delivered to Legal Counsel and the Purchasers by facsimile on the

same day of such effectiveness and by overnight mail), (ii) of any request by the Commission for amendments or supplements to a Registration Statement or related prospectus or related information, and (iii) of the Company's reasonable determination that a post-effective amendment to a Registration Statement would be appropriate.

(g) The Company shall use its best efforts to prevent the issuance of any stop order or other suspension of effectiveness of a Registration Statement, or the suspension of the qualification of any of the Registrable Securities for sale in any jurisdiction and, if such an order or suspension is issued, to obtain the withdrawal of such order or suspension at the earliest possible moment and to notify Legal Counsel and the Purchaser who holds Registrable Securities being sold of the issuance of such order and the resolution thereof or its receipt of notice of the initiation or threat of any proceeding for such purpose.

(h) If a Purchaser is required under applicable securities law to be described in the Registration Statement as an underwriter, at the reasonable request of the Purchaser, the Company shall furnish to the Purchaser, on the date of the effectiveness of the Registration Statement and thereafter from time to time on such dates as the Purchaser may reasonably request (i) a letter, dated such date, from the Company's independent certified public accountants in form and substance as is customarily given by independent certified public accountants to underwriters in an underwritten public offering, addressed to the Purchaser, and (ii) an opinion, dated as of such date, of counsel representing the Company for purposes of such Registration Statement, in form, scope and substance as is customarily given in an underwritten public offering, addressed to the Purchaser.

(i) If a Purchaser is required under applicable securities law to be described in the Registration Statement as an underwriter, upon the written request of the Purchaser in connection with the Purchaser's due diligence requirements, if any, the Company shall make available for inspection by (i) the Purchaser, (ii) Legal Counsel and (iii) one firm of accountants or other agents retained by the Purchaser (collectively, the "***Inspectors***"), all pertinent financial and other records, and pertinent corporate documents and properties of the Company (collectively, the "***Records***"), as shall be reasonably deemed necessary by each Inspector, and cause the Company's officers, directors and employees to supply all information which any Inspector may reasonably request; provided, however, that each Inspector shall agree to hold in strict confidence and shall not make any disclosure (except to the Purchaser) or use of any Record or other information which the Company determines in good faith to be confidential, and of which determination the Inspectors are so notified, unless (a) the disclosure of such Records is necessary to avoid or correct a misstatement or omission in any Registration Statement or is otherwise required under the Securities Act, (b) the release of such Records is ordered pursuant to a final, non-appealable subpoena or order from a court or government body of competent jurisdiction, or (c) the information in such Records has been made generally available to the public other than by disclosure in violation of this or any other Transaction Document. The Purchaser agrees that it shall, upon learning that disclosure of such Records is sought in or by a court or governmental body of competent jurisdiction or through other means, give prompt notice to the Company and allow the

Company, at its expense, to undertake appropriate action to prevent disclosure of, or to obtain a protective order for, the Records deemed confidential. Nothing herein (or in any other confidentiality agreement between the Company and the Purchaser) shall be deemed to limit the Purchaser's ability to sell Registrable Securities in a manner which is otherwise consistent with applicable laws and regulations.

(j) The Company shall hold in confidence and not make any disclosure of information concerning the Purchasers provided to the Company unless (i) disclosure of such information is necessary to comply with federal or state securities laws, (ii) the disclosure of such information is necessary to avoid or correct a misstatement or omission in any Registration Statement, (iii) the release of such information is ordered pursuant to a subpoena or other final, non-appealable order from a court or governmental body of competent jurisdiction or (iv) such information has been made generally available to the public other than by disclosure in violation of this Agreement or any other agreement. The Company agrees that it shall, upon learning that disclosure of such information concerning the Purchasers is sought in or by a court or governmental body of competent jurisdiction or through other means, give prompt written notice to the Purchasers and allow the Purchasers, at each Purchaser's expense, to undertake appropriate action to prevent disclosure of, or to obtain a protective order for, such information.

(k) The Company shall use its best efforts to cause all of the Registrable Securities covered by a Registration Statement to be listed on each securities exchange on which securities of the same class or series issued by the Company are then listed, if any, if the listing of such Registrable Securities is then permitted under the rules of such exchange. The Company shall pay all fees and expenses in connection with satisfying its obligation under this Section 11.6(k).

(l) The Company shall cooperate with the Purchasers and, to the extent applicable, facilitate the timely preparation and delivery of certificates (not bearing any restrictive legend) representing the Registrable Securities to be offered pursuant to a Registration Statement and enable such certificates to be in such denominations or amounts, as the case may be, as the Purchasers may reasonably request and registered in such names as the Purchasers may request.

(m) If requested by a Purchaser, the Company shall (i) as soon as practicable incorporate in a prospectus supplement or post-effective amendment such information as the Purchaser reasonably requests to be included therein relating to the sale and distribution of Registrable Securities, including, without limitation, information with respect to the number of Registrable Securities being offered or sold, the purchase price being paid therefor and any other terms of the offering of the Registrable Securities to be sold in such offering; (ii) as soon as practicable make all required filings of such prospectus supplement or post-effective amendment after being notified of the matters to be incorporated in such prospectus supplement or post-effective amendment; and (iii) as soon as practicable, supplement or make amendments to any Registration Statement if reasonably requested by the Purchaser.

(n) The Company shall use its best efforts to cause the Registrable Securities covered by a Registration Statement to be registered with or approved by such other governmental agencies or authorities as may be necessary to consummate the disposition of such Registrable Securities.

(o) The Company shall otherwise use its best efforts to comply with all applicable rules and regulations of the Commission in connection with any registration hereunder.

(p) Within two (2) Business Days after a Registration Statement which covers Registrable Securities is ordered effective by the Commission, the Company shall deliver, and shall cause legal counsel for the Company to deliver, to the transfer agent for such Registrable Securities (with copies to the Purchasers) confirmation that such Registration Statement has been declared effective by the Commission.

(q) Notwithstanding anything to the contrary herein, at any time after the Effective Date, the Company may delay the disclosure of material, non-public information concerning the Company the disclosure of which at the time is not, in the good faith opinion of the Board of Directors and its counsel, in the best interest of the Company and, in the opinion of counsel to the Company, otherwise required (a "***Grace Period***"); provided, that the Company shall promptly (i) notify the Purchasers in writing of the existence of material, non-public information giving rise to a Grace Period (provided that in each notice the Company will not disclose the content of such material, non-public information to the Purchasers) and the date on which the Grace Period will begin, and (ii) notify the Purchasers in writing of the date on which the Grace Period ends; and, provided further, that the Grace Periods shall not exceed an aggregate of ten (10) Trading Days during any three hundred sixty five (365) day period and the first day of any Grace Period must be at least thirty (30) days after the last day of any prior Grace Period (each, an "***Allowable Grace Period***"). For purposes of determining the length of a Grace Period above, the Grace Period shall begin on and include the date the Purchasers receive the notice referred to in clause (i) and shall end on and include the later of the date the Purchasers receive the notice referred to in clause (ii) and the date referred to in such notice. The provisions of Section 11.6(g) hereof shall not be applicable during the period of any Allowable Grace Period. Upon expiration of the Grace Period, the Company shall again be bound by the first sentence of Section 11.6(f) with respect to the information giving rise thereto unless such material, non-public information is no longer applicable. Notwithstanding anything to the contrary, the Company shall cause its transfer agent to deliver unlegended shares of Common Stock to a transferee of any Purchaser in accordance with the terms of this Agreement in connection with any sale of Registrable Securities with respect to which a Purchaser has entered into a contract for sale, and delivered a copy of the prospectus included as part of the applicable Registration Statement (unless an exemption from such prospectus delivery requirement exists), prior to the Purchaser's receipt of the notice of a Grace Period and for which the Purchaser has not yet settled.

11.7. Obligations of the Purchasers.

(a) At least five (5) Business Days prior to the first anticipated filing date of a Registration Statement, the Company shall notify each Purchaser in writing of the information the Company requires from such Purchaser in order to have that Purchaser's Registrable Securities included in such Registration Statement. It shall be a condition precedent to the obligations of the Company to complete the registration pursuant to this Agreement with respect to the Registrable Securities of a particular Purchaser that the Purchaser shall furnish to the Company such information regarding itself, the Registrable Securities held by it and the intended method of disposition of the Registrable Securities held by it as shall be reasonably required to effect the effectiveness of the registration of such Registrable Securities and shall execute such documents in connection with such registration as the Company may reasonably request.

(b) Each Purchaser, by its acceptance of the Registrable Securities, agrees to cooperate with the Company as reasonably requested by the Company in connection with the preparation and filing of any Registration Statement hereunder, unless the Purchaser has notified the Company in writing of the Purchaser's election to exclude all of the Purchaser's Registrable Securities from such Registration Statement.

(c) Each Purchaser agrees that, upon receipt of any notice from the Company of the happening of any event of the kind described in Section 11.6(g) or the first sentence of 11.6(f), the Purchaser will immediately discontinue disposition of Registrable Securities pursuant to any Registration Statement(s) covering such Registrable Securities until the Purchaser's receipt of the copies of the supplemented or amended prospectus contemplated by Section 11.6(g) or the first sentence of 11.6(f) or receipt of notice that no supplement or amendment is required. Notwithstanding anything to the contrary, the Company shall cause its transfer agent to deliver unlegended shares of Common Stock to a transferee of the Purchaser in accordance with the terms of this Agreement in connection with any sale of Registrable Securities with respect to which the Purchaser has entered into a contract for sale prior to the Purchaser's receipt of a notice from the Company of the happening of any event of the kind described in Section 11.6(g) or the first sentence of 11.6(f) and for which the Purchaser has not yet settled.

(d) Each Purchaser covenants and agrees that it will comply with the prospectus delivery requirements of the Securities Act as applicable to it or an exemption therefrom in connection with sales of Registrable Securities pursuant to the Registration Statement.

11.8. Expenses of Registration. All reasonable expenses, other than underwriting discounts and commissions incurred in connection with registrations, filings or qualifications pursuant to Section 11.5 and Section 11.6, including, without limitation, all registration, listing and qualifications fees, printers and accounting fees, and fees and disbursements of counsel for the Company, shall be paid by the Company.

11.9. Reports under the Exchange Act. With a view to making available to the Purchasers the benefits of Rule 144 promulgated under the Securities Act or any other similar

rule or regulation of the Commission that may at any time permit the Purchasers to sell securities of the Company to the public without registration ("***Rule 144***"), the Company agrees to:

(a) make and keep public information available, as those terms are understood and defined in Rule 144;

(b) file with the Commission in a timely manner all reports and other documents required of the Company under the Exchange Act so long as the Company remains subject to such requirements and the filing of such reports and other documents is required for the applicable provisions of Rule 144; and

(c) furnish to the Purchasers so long as any Purchaser owns Registrable Securities, promptly upon request, (i) a written statement by the Company, if true, that it has complied with the reporting requirements of Rule 144, the Securities Act and the Exchange Act, (ii) a copy of the most recent annual or quarterly report of the Company and such other reports and documents so filed by the Company and (iii) such other information as may be reasonably requested to permit the Purchasers to sell such securities pursuant to Rule 144 without registration.

11.10. Piggyback Rights. Whenever the Company proposes to register any of its Common Stock or securities convertible into Common Stock, whether or not for its own account, provided such offering shall be underwritten or placed by a placement agent, the Company will give prompt written notice to the Purchasers of its intention to effect such a registration (but in no event less than fifteen (15) Business Days prior to the anticipated filing date) and will include in such registration all Registrable Securities with respect to which the Company has received written requests for inclusion therein within ten (10) Business Days after the date of the Company's notice (a "***Piggyback Registration***"). Any Purchaser may withdraw its Registrable Securities from such Piggyback Registration by giving written notice to the Company and the managing underwriter, if any, on or before the fifth Business Day prior to the planned effective date of such Piggyback Registration. The Company may terminate or withdraw any registration under this Section 11.10 prior to the effectiveness of such registration, whether or not the Purchaser has elected to include Registrable Securities in such registration. If a Piggyback Registration relates to an underwritten primary offering on behalf of the Company, and the managing underwriters advise the Company that in their reasonable opinion the number of securities requested to be included in such registration exceeds the number which can be sold without adversely affecting the marketability of such offering (including an adverse effect on the per share offering price), the Company will include in such registration or prospectus only such number of securities that in the reasonable opinion of such underwriters can be sold without adversely affecting the marketability of the offering (including an adverse effect on the per share offering price), *provided*, without the consent of the Purchaser, such number so included shall equal at least 30% of such Purchaser's Registrable Securities.

11.11. Assignment of Registration Rights. The rights under this Section 11 shall be automatically assignable by a Purchaser to any transferee of all or any portion of the Purchaser's Registrable Securities if: (i) the Purchaser agrees in writing with the transferee or assignee to assign such rights and a copy of such agreement is furnished to the Company within a reasonable time after such assignment; (ii) the Company is, within a reasonable time after such

transfer or assignment, furnished with written notice of (a) the name and address of such transferee or assignee and (b) the securities with respect to which such registration rights are being transferred or assigned; (iii) immediately following such transfer or assignment the further disposition of such securities by the transferee or assignee is restricted under the Securities Act or applicable state securities laws; (iv) at or before the time the Company receives the written notice contemplated by clause (ii) of this sentence the transferee or assignee agrees in writing with the Company to be bound by all of the provisions contained herein; and (v) such transfer shall have been made in accordance with the applicable requirements of this Agreement.

11.12. Indemnification.

(a) Company Indemnification. The Company will indemnify each Purchaser who holds Registrable Securities (if Registrable Securities held by such Purchaser are included in the securities as to which such registration is being effected), each of its officers and directors, partners, members and each person controlling such Purchaser within the meaning of Section 15 of the Securities Act, against all expenses, claims, losses, damages or liabilities (or actions in respect thereof), including any of the foregoing incurred in settlement of any litigation, commenced or threatened, arising out of or based on (A) any untrue statement (or alleged untrue statement) of a material fact contained in any Registration Statement, prospectus, offering circular or other document, or any amendment or supplement thereto, incident to any such Registration Statement, or based on any omission (or alleged omission) to state therein a material fact required to be stated therein or necessary to make the statements therein, in light of the circumstances in which they were made, not misleading, or (B) any violation by the Company of the Securities Act, the Exchange Act, state securities laws or any rule or regulation promulgated under such laws applicable to the Company in connection with any such registration, and in each case, the Company will reimburse each such Purchaser, each of its officers and directors, partners, members and each person controlling such Purchaser, for any legal and any other expenses reasonably incurred, as such expenses are incurred, in connection with investigating, preparing or defending any such claim, loss, damage, liability or action, *provided* that the Company will not be liable in any such case to the extent that any such claim, loss, damage, liability or expense arises out of or is based on (X) any untrue statement or omission or alleged untrue statement or omission made in reliance upon and in conformity with written information furnished to the Company by an instrument duly executed by such Purchaser or controlling person, and stated to be specifically for use therein, (Y) the use by a Purchaser of an outdated or defective prospectus after the Company has notified such Purchaser in writing that the prospectus is outdated or defective or (Z) a Purchaser's (or any other indemnified person's) failure to send or give a copy of the prospectus or supplement (as then amended or supplemented), if required, pursuant to Rule 172 under the Securities Act (or any successor rule) to the Persons asserting an untrue statement or alleged untrue statement or alleged untrue statement or omission or alleged omission at or prior to the written confirmation of the sale of Registrable Securities to such person if such statement or omission was corrected in such prospectus or supplement; *provided, further,* that the indemnity agreement contained in this Section 11.12(a) shall not apply to amounts paid in settlement of any such loss, claim, damage, liability or action if such settlement is effected without the consent of the Company (which consent shall not be unreasonably withheld).

(b) Purchaser Indemnification. Each Purchaser holding Registrable Securities will, if Registrable Securities held by such Purchaser are included in the securities as to which such registration is being effected, severally and not jointly, indemnify the Company, each of its directors and officers, other holders of the Company's securities covered by such Registration Statement, each person who controls the Company within the meaning of Section 15 of the Securities Act, and each such holder, each of its officers and directors and each person controlling such holder within the meaning of Section 15 of the Securities Act, against all claims, losses, damages and liabilities (or actions in respect thereof) arising out of or based on: (A) any untrue statement (or alleged untrue statement) of a material fact contained in any such Registration Statement, prospectus, offering circular or other document, or any omission (or alleged omission) to state therein a material fact required to be stated therein or necessary to make the statements therein not misleading, to the extent, and only to the extent, that such untrue statement (or alleged untrue statement) or omission (or alleged omission) is made in such Registration Statement, prospectus, offering circular or other document in reliance upon and in conformity with written information furnished to the Company by an instrument duly executed by such Purchaser and stated to be specifically for use therein, or (B) any violation by such Purchaser of the Securities Act, the Exchange Act, state securities laws or any rule or regulation promulgated under such laws applicable to such Purchaser, and in each case, such Purchaser will reimburse the Company, each other holder, and directors, officers, persons, underwriters or control persons of the Company and the other holders for any legal or any other expenses reasonably incurred, as such expenses are incurred, in connection with investigating or defending any such claim, loss, damage, liability or action; *provided*, that the indemnity agreement contained in this Subsection 11.12(b) shall not apply to amounts paid in settlement of any such loss, claim, damage, liability or action if such settlement is effected without the consent of such indemnifying Purchaser (which consent shall not be unreasonably withheld or delayed). The liability of any Purchaser for indemnification under this Section 11.12(b) in its capacity as a seller of Registrable Securities shall not exceed the amount of net proceeds to such Purchaser of the securities sold in any such registration.

(c) Notice and Procedure. Each party entitled to indemnification under this Section 11.12 (the "***Indemnified Party***") shall give written notice to the party required to provide indemnification (the "***Indemnifying Party***") promptly after such Indemnified Party has actual knowledge of any claim as to which indemnity may be sought, and shall permit the Indemnifying Party to assume the defense of any such claim or any litigation resulting therefrom, provided that counsel for the Indemnifying Party, who shall conduct the defense of such claim or litigation, shall be approved by the Indemnified Party (whose approval shall not unreasonably be withheld), and the Indemnified Party may participate in such defense at such party's expense, and provided further that the failure of any Indemnified Party to give notice as provided herein shall not relieve the Indemnifying Party of its obligations under this Agreement unless the failure to give such notice is materially prejudicial to an Indemnifying Party's ability to defend such action and provided further, that the Indemnifying Party shall not assume the defense for matters as to which there is a conflict of interest or there are separate and different defenses. No Indemnifying Party, in the defense of any such claim or litigation,

shall, except with the consent of each Indemnified Party (whose consent shall not be unreasonably withheld), consent to entry of any judgment or enter into any settlement which does not include as an unconditional term thereof the giving by the claimant or plaintiff to such Indemnified Party of a release from all liability in respect to such claim or litigation.

(d) Contribution. If the indemnification provided for in this Section 11.12 is held by a court of competent jurisdiction to be unavailable to an Indemnified Party with respect to any losses, claims, damages or liabilities referred to herein, the Indemnifying Party, in lieu of indemnifying such Indemnified Party thereunder, shall to the extent permitted by applicable law contribute to the amount paid or payable by such Indemnified Party as a result of such loss, claim, damage or liability in such proportion as is appropriate to reflect the relative fault of the Indemnifying Party on the one hand and of the Indemnified Party on the other in connection with the untrue statement or omission that resulted in such loss, claim, damage or liability, as well as any other relevant equitable considerations. The relative fault of the Indemnifying Party and of the Indemnified Party shall be determined by a court of law by reference to, among other things, whether the untrue or alleged untrue statement of a material fact or the omission to state a material fact relates to information supplied by the Indemnifying Party or by the Indemnified Party and the parties' relative intent, knowledge, access to information and opportunity to correct or prevent such statement or omission; provided, that in no event shall any contribution by a Purchaser hereunder exceed the proceeds from the offering received by such Purchaser. The amount paid or payable by a party as a result of any loss, claim, damage or liability shall be deemed to include, subject to the limitations set forth in this Agreement, any reasonable attorneys' or other reasonable fees or expenses incurred by such party in connection with any proceeding to the extent such party would have been indemnified for such fees or expenses if the indemnification provided for in this Section 11.12 was available to such party in accordance with its terms.

(e) Survival. The obligations of the Company and the Purchasers under this Section 11.12 shall survive completion of any offering of Registrable Securities in a Registration Statement and the termination of this Agreement. The indemnity and contribution agreements contained in this Section 11.12 are in addition to any liability that the Indemnifying Parties may have to the Indemnified Parties and are not in diminution or limitation of other remedies or causes of action that the parties may have under the Transaction Documents.

12. Definitions. Unless the context otherwise requires, the terms defined in this Section 12 shall have the meanings specified for all purposes of this Agreement.

Except as otherwise expressly provided, all accounting terms used in this Agreement, whether or not defined in this Section 12, shall be construed in accordance with GAAP. If the Company has one or more Subsidiaries, such accounting terms shall be determined on a consolidated basis for the Company and each of its Subsidiaries, and the financial statements and other financial information to be furnished by the Company pursuant to this Agreement shall be

consolidated and presented with consolidating financial statements of the Company and each of its Subsidiaries.

"2002 Stock Incentive Plan" has the meaning assigned to it in Section 5.1(a) hereof.

"2007 Equity Incentive Plan" has the meaning assigned to it in Section 5.1(a) hereof.

"Additional Notes" has the meaning assigned to it in Section 3.2 hereof.

"Affiliate" shall have the meaning ascribed to such term in Rule 12b-2 of the General Rules and Regulations under the Exchange Act.

"Agreement" has the meaning assigned to it in the introductory paragraph hereof.

"Allowable Grace Period" has the meaning assigned to it in Section 11.6 hereof.

"Applicable Law" has the meaning assigned to it in Section 5.18 hereof.

"Authorizations" has the meaning assigned to it in Section 5.18 hereof.

"Board of Directors" has the meaning assigned to it in Section 5.1(a) hereof.

"Business Day" has the meaning assigned to it in Section 6.5 hereof.

"Charter Documents" has the meaning assigned to it in Section 5.8 hereof.

"Closing" has the meaning assigned to it in Section 3.1 hereof.

"Closing Date" has the meaning assigned to it in Section 3.2 hereof.

"Code" means the Internal Revenue Code of 1986, as amended.

"Commission" means the Securities and Exchange Commission.

"Commitment Amount" has the meaning assigned to it in the recitals hereof.

"Common Stock" has the meaning assigned to it in the recitals hereof.

"Company" has the meaning assigned to it in the introductory paragraph.

"Company Intellectual Property" has the meaning assigned to it in Section 5.21(a) hereof.

"Contingent Obligation" means, as to any Person, any direct or indirect liability, contingent or otherwise, of that Person with respect to any indebtedness, lease, dividend or other obligation of another Person if the primary purpose or intent of the Person incurring such liability, or the primary effect thereof, is to provide assurance to the obligee of such liability that

such liability will be paid or discharged, or that any agreements relating thereto will be complied with, or that the holders of such liability will be protected (in whole or in part) against loss with respect thereto.

"Control Agreement" has the meaning assigned to it in the Security Agreement.

"Conversion Shares" has the meaning assigned to it in the recitals hereof.

"Disclosure Schedule" has the meaning assigned to it in Section 5 hereof.

"Domain Names" has the meaning assigned to it in Section 5.21(c) hereof.

"DTC" has the meaning assigned to it in Section 9.2 hereof.

"Effective Date" means the date the Registration Statement pursuant to Section 11 has been declared effective by the Commission.

"Effectiveness Deadline" has the meaning assigned to it in Section 11.1 hereof.

"Effectiveness Failure" has the meaning assigned to it in Section 11.5 hereof.

"Employee Benefit Plan" has the meaning assigned to it in Section 5.17(b) hereof.

"Encumbrances" has the meaning assigned to it in Section 5.2 hereof.

"Environmental Laws" has the meaning assigned to it in Section 5.20(b) hereof.

"ERISA" has the meaning assigned to it in Section 5.17(a) hereof.

"Employee Benefit Plan" has the meaning assigned to it in Section 5.17(b) hereof.

"ESPP" has the meaning assigned to it in Section 5.1 hereof.

"Exchange Act" means the Securities Exchange Act of 1934, as amended.

"Exempt Issuance" means the issuance of (a) shares of Common Stock or options to Company employees, officers, directors or consultants pursuant to any stock or option plan duly adopted by a majority of the non-employee members of the Board of Directors of the Company, (b) the Notes that may be issued pursuant to the Transaction Documents and any securities upon the exchange or conversion of the Notes (including the Conversion Shares, the Additional Notes and Notes issued on payment of PIK Interest) and/or other securities exercisable or exchangeable for or convertible into shares of Common Stock issued and outstanding on the date of this Agreement, or (c) securities issued pursuant to acquisitions or strategic transactions approved by a majority of the disinterested directors, but shall not include a transaction to an entity whose primary business is investing in securities.

"Exercise Period" has the meaning assigned to it in Section 10.3 hereof.

"FDA" has the meaning assigned to it in Section 5.18 hereof.

“FFDCA” has the meaning assigned to it in Section 5.18 hereof.

“Filing Deadline” has the meaning assigned to it in Section 11.1 hereof.

“Filing Failure” has the meaning assigned to it in Section 11.5 hereof.

“FINRA” means the Financial Industry Regulatory Authority.

“Follow-on Offering” has the meaning assigned to it in Section 6.15 hereof.

“GAAP” means U.S. generally accepted accounting principles consistently applied.

“Grace Period” has the meaning assigned to it in Section 11.6(q) hereof.

“Governmental Entity” means any national, federal, state, municipal, local, territorial, foreign or other government or any department, commission, board, bureau, agency, regulatory authority or instrumentality thereof, or any court, judicial, administrative or arbitral body or public or private tribunal.

“Hazardous Material” has the meaning assigned to it in Section 5.20(b) hereof.

“Increase Deadline” has the meaning assigned to it in Section 6.12 hereof.

“Indebtedness” has the meaning assigned in the Notes.

“Initial Closing” has the meaning assigned to it in Section 3.1 hereof.

“Initial Closing Date” has the meaning assigned to it in Section 3.1 hereof.

“Inspectors” has the meaning assigned to it in Section 11.6(i).

“Intellectual Property” has the meaning assigned to it in Section 5.21(a) hereof.

“Interest Share Calculation” shall have the meaning assigned to it in the definition of Required Registration Amount hereof.

“IP Summary” has the meaning assigned to it in Section 5.21(b) hereof.

“Issuance Notice” has the meaning assigned to it in Section 10.2 hereof.

“Key Employee” means each of the Company’s executive officers.

“Knowledge” by a Person of a particular fact or other matter means the following: (a) if the Person is an individual, that such individual is actually aware or reasonably should be aware, after due inquiry, by virtue of such person’s office, of such fact or other matter; and (b) if the Person is an Entity, any executive officer of such Person is actually aware or reasonably should be aware, after due inquiry, of such fact or other matter.

“Legal Counsel” has the meaning assigned to it in Section 11.2

“Maintenance Failure” has the meaning assigned to it in Section 11.5 hereof.

“Material Adverse Effect” means any (i) adverse effect on the issuance or validity of the Securities or the transactions contemplated hereby or on the ability of the Company to perform its obligations under this Agreement or the other Transaction Documents, or (ii) material adverse effect on the condition (financial or otherwise), prospects, properties, assets, liabilities, business or operations of the Company.

“Material Contract” means all written and oral contracts, agreements, deeds, mortgages, leases, subleases, licenses, instruments, notes, commitments, commissions, undertakings, arrangements and understandings (i) which by their terms involve, or would reasonably be expected to involve, aggregate payments by or to the Company during any twelve month period in excess of $50,000, (ii) the breach of which by the Company would reasonably be expected to have a Material Adverse Effect, (iii) which are required to be filed as exhibits by the Company with the Commission pursuant to Items 601(b)(2), 601(b)(4) or 601(b)(10) of Regulation S-K promulgated by the Commission or (iv) the License Agreement with Sanofi-Aventis, dated March 19, 1992.

“Material Permits” has the meaning assigned to it in Section 5.28 hereof.

“New Securities” has the meaning assigned to it in Section 10.1 hereof.

“Non-Qualified Stock Plan” has the meaning assigned to it in Section 5.1(a) hereof.

“Note Purchase Price” has the meaning assigned to it in Section 2 hereof.

“Notes” has the meaning assigned to it in the recitals hereof.

“OUM” has the meaning assigned to it in Section 5.34 hereof.

“Person” means and includes all natural persons, corporations, business trusts, associations, companies, partnerships, joint ventures, limited liability companies and other entities and governments and agencies and political subdivisions.

“Permitted Indebtedness” has the meaning assigned in the Notes.

“Permitted Liens” has the meaning assigned in the Notes.

“Piggyback Registration” has the meaning assigned to it in Section 11.10 hereof.

“Preemptive Portion” has the meaning assigned to it in Section 10.1 hereof.

“Preferred Stock” has the meaning assigned to it in Section 5.1(a) hereof.

“Preferred Shareholders Rights Agreement” has the meaning assigned to it in Section 5.1(a) hereof.

"Pro Rata Interest" means the relative interests of the Purchasers, as set forth on Schedule I attached hereto.

"Purchaser" has the meaning assigned to it in the introductory paragraph of this Agreement and shall include any Affiliates of the Purchaser.

"Records" has the meaning assigned to it in Section 11.6(i).

"Registrable Securities" has the meaning assigned to it in Section 11.1 hereof.

"Registration Delay Payments" has the meaning assigned to it in Section 11.5 hereof.

"Registration Period" has the meaning assigned to it in Section 11.6(a).

"Registration Statement" means a registration statement or registration statements of the Company filed under the Securities Act pursuant to Section 11 hereof.

"Regulation D" has the meaning assigned to it in the recitals hereof.

"Reporting Period" has the meaning assigned to it in Section 6.3 hereof.

"Required Registration Amount" for the Registration Statement pursuant to Section 11 means, solely for the purposes of calculating the number of shares of Common Stock covering the Registrable Securities on the Registration Statement, the sum of (i) the aggregate of the maximum number of Conversion Shares issued and issuable pursuant to the Notes (including, for the avoidance of doubt, the Notes issued at the Initial Closing, plus the full amount of the Additional Notes potentially issuable hereunder), and (ii) the aggregate of the maximum number of Conversion Shares issued and issuable pursuant to Notes that may be issued in satisfaction of PIK Interest, in each case at the then applicable Conversion Price as of the Trading Day (as defined in the Notes) immediately preceding the applicable date of determination, all subject to adjustment in accordance with Section 11.4 (without regard to any limitations on conversion of the Notes).

"Rule 144" has the meaning assigned to it in Section 11.9 hereof.

"SEC Reports" has the meaning assigned to it in Section 5.13(a) hereof.

"Securities" has the meaning assigned to it in Section 1 hereof.

"Securities Act" has the meaning assigned to it in the recitals hereof.

"Security Agreement" has the meaning assigned to in Section 1 hereof.

"Subsequent Closing" has the meaning assigned to it in Section 3.2 hereof.

"Subsequent Closing Date" has the meaning assigned to it in Section 3.2 hereof.

"Subsidiary" means any corporation, association trust, limited liability company, partnership, joint venture or other business association or entity (i) at least 50% of the outstanding voting securities of which are at the time owned or controlled directly or indirectly by the Company or (ii) with respect to which the Company possesses, directly or indirectly, the power to direct or cause the direction of the affairs or management of such Person.

"Test Trading Day" has the meaning assigned to it in Section 11.4 hereof.

"Total Notes Purchase Price" shall mean $4,500,000.

"Trading Market" means the following markets or exchanges on which the Common Stock is listed or quoted for trading on the date in question: the American Stock Exchange, the Nasdaq Capital Market, the Nasdaq Global Market, the Nasdaq Global Select Market, the New York Stock Exchange or the OTC Markets Group Inc.

"Transaction Documents" means this Agreement, the Note(s) and the Security Agreement.

13. Enforcement.

13.1. Cumulative Remedies. None of the rights, powers or remedies conferred upon the Purchasers on the one hand or the Company on the other hand shall be mutually exclusive, and each such right, power or remedy shall be cumulative and in addition to every other right, power or remedy, whether conferred by this Agreement, any of the other Transaction Documents or now or hereafter available at law, in equity, by statute or otherwise.

13.2. No Implied Waiver. Except as expressly provided in this Agreement, no course of dealing between the Company and the Purchasers or any other holder of shares of Common Stock and no delay in exercising any such right, power or remedy conferred hereby or by any of the other Transaction Documents or now or hereafter existing at law in equity, by statute or otherwise, shall operate as a waiver of, or otherwise prejudice, any such right, power or remedy.

14. Confidentiality. Except as otherwise agreed in writing by the Company, each Purchaser agrees that it will use reasonable care to keep confidential and not disclose, divulge, or use for any purpose (other than to monitor its investment in the Company) any confidential information obtained from the Company pursuant to the terms of the Transaction Documents (including notice of the Company's intention to file a registration statement), unless such confidential information (a) is known or becomes known to the public in general (other than as a result of a breach of this Section 14 by the Purchaser), (b) is or has been independently developed or conceived by the Purchaser without use of the Company's confidential information, (c) is or has been made known or disclosed to the Purchaser by a third party without knowledge by the Purchaser of any obligation of confidentiality such third party owes to the Company with respect to the information or (d) was known to the Purchaser prior to disclosure to the Purchaser by the Company; provided, however, that the Purchaser may disclose confidential information (i) to its attorneys, accountants, consultants, and other professionals to the extent necessary to obtain their services in connection with monitoring its investment in the Company provided that the Purchaser informs such person that such information is confidential and directs such person to

maintain the confidentiality of such information; (ii) to any prospective purchaser of any Securities from the Purchaser, if such prospective purchaser agrees to be bound by the provisions of this Section 14; (iii) to any Affiliate, partner, member, stockholder or advisor of the Purchaser in the ordinary course of business, provided that the Purchaser informs such person that such information is confidential and directs such person to maintain the confidentiality of such information; or (iv) as may otherwise be required by law, provided that the Purchaser promptly notifies the Company of such disclosure and, if requested by the Company, reasonably cooperates with the Company at the Company's sole expense to minimize the extent of any such required disclosure. Notwithstanding anything to the contrary herein, the confidentiality obligations of this Section 14 shall survive the termination of this Agreement.

15. Miscellaneous.

15.1. Waivers and Amendments. Upon the approval of the Company and the written consent of the Required Holders, the obligations of the Company and the rights of the Purchasers under this Agreement may be waived (either generally or in a particular instance, either retroactively or prospectively and either for a specified period of time or indefinitely). Neither this Agreement, nor any provision hereof, maybe changed, waived, discharged or terminated orally or by course of dealing, but only by an instrument in writing executed by the Company and the Required Holders.

15.2. Notices. All notices, requests, consents, and other communications under this Agreement shall be in writing and shall be deemed delivered (a) when delivered, if delivered personally, (b) four business days after being sent by registered or certified mail, return receipt requested, postage prepaid; (c) one business day after being sent via a reputable nationwide overnight courier service guaranteeing next business day delivery, or (d) when receipt is acknowledged, in the case of facsimile, in each case to the intended recipient as set forth below, with respect to the Company, and to the addresses set forth on Schedule I with respect to the Purchasers.

If to the Company:

A.P. Pharma, Inc.
123 Saginaw Drive
Redwood City, CA 94063
Attention: John Whelan
Facsimile No.: (650) 365-6490

with a copy to:

Latham & Watkins LLP
140 Scott Drive
Menlo Park, California 94025
Attention: Alan C. Mendelson, Esq.
Facsimile No.: (650) 463-2600

or at such other address as the Company or each Purchaser each may specify by written notice to the other parties hereto in accordance with this Section 15.2.

15.3. Indemnification. The Company shall indemnify, save and hold harmless each Purchaser and its directors, officers, employees, partners, representatives and agents from and against (and shall promptly reimburse such indemnified persons for) any and all liability, loss, cost, damage, reasonable attorneys' and accountants' fees and expenses, court costs and all other out-of-pocket expenses incurred in connection with or arising from claims, actions, suits, proceedings or similar claims by any Person or entity (other than such Purchaser) associated or relating to the execution, delivery and performance of this Agreement, any of the other Transaction Documents or the transactions contemplated hereby or thereby or the exercise by the Purchaser of its rights thereunder. This indemnification provision shall be in addition to the rights of each Purchaser to bring an action against the Company for breach of any term of this Agreement or the other Transaction Documents.

15.4. No Waivers. No failure or delay by any party in exercising any right, power or privilege hereunder shall operate as a waiver thereof nor shall any single or partial exercise thereof preclude any other or further exercise thereof or the exercise of any other right, power or privilege. The rights and remedies herein provided shall be cumulative and not exclusive of any rights or remedies provided by law.

15.5. Successors and Assigns. All the terms and provisions of this Agreement shall be binding upon and inure to the benefit of and be enforceable by the respective parties hereto, the successors and permitted assigns of each Purchaser and the successors of the Company, whether so expressed or not. None of the parties hereto may assign its rights or obligations hereof without the prior written consent of the Company, except that a Purchaser may, without the prior consent of the Company, assign its rights to purchase the Securities hereunder to any of its Affiliates (provided such Affiliate agrees to be bound by the terms of this Agreement and makes the same representations and warranties set forth in Section 4 hereof). This Agreement shall not inure to the benefit of or be enforceable by any other Person.

15.6. Headings. The headings of the Sections and paragraphs of this Agreement have been inserted for convenience of reference only and do not constitute a part of this Agreement.

15.7. Governing Law. This Agreement shall be governed by and construed in accordance with the laws of the State of California without regard to its conflict of law principles.

15.8. Jurisdiction. Any suit, action or proceeding seeking to enforce any provision of, or based on any matter arising out of or in connection with, this Agreement or the transactions contemplated hereby shall be brought in any federal or state court located in the City and County of San Diego, California, and each of the parties hereby consents to the jurisdiction of such courts (and of the appropriate appellate courts therefrom) in any such suit, action or proceeding and irrevocably waives, to the fullest extent permitted by law, any objection which it may now or hereafter have to the laying of the venue of any such suit, action or proceeding in any such court or that any such suit, action or proceeding which is brought in any such court has been brought in an inconvenient forum. Process in any such suit, action or proceeding may be served on any party anywhere in the world, whether within or without the jurisdiction of any

such court. Without limiting the foregoing, each party agrees that service of process on such party as provided in Section 15.2 shall be deemed effective service of process on such party.

15.9. Waiver of Jury Trial. TO THE EXTENT NOT PROHIBITED BY APPLICABLE LAW WHICH CANNOT BE WAIVED, THE PURCHASERS AND THE COMPANY HEREBY WAIVE AND COVENANT THAT NEITHER THE COMPANY NOR THE PURCHASERS WILL ASSERT, ANY RIGHT TO TRIAL BY JURY ON ANY ISSUE IN ANY PROCEEDING, WHETHER AS PLAINTIFF, DEFENDANT OR OTHERWISE, IN RESPECT OF ANY ISSUE, CLAIM, DEMAND, ACTION OR CAUSE OF ACTION ARISING OUT OF OR BASED UPON THIS AGREEMENT, ANY OTHER AGREEMENT OR THE SUBJECT MATTER HEREOF OR THEREOF OR IN ANY WAY CONNECTED WITH, RELATED OR INCIDENTAL TO THE DEALINGS OF THE PURCHASER AND THE COMPANY HEREUNDER OR THEREUNDER, IN EACH CASE WHETHER NOW EXISTING OR HEREAFTER ARISING AND WHETHER IN TORT OR CONTRACT OR OTHERWISE. The Company acknowledges that it has been informed by the Purchasers that the provisions of this Section 15.9 constitute a material inducement upon which the Purchaser are relying and will rely in entering into this Agreement. The Purchaser or the Company may file an original counterpart or a copy of this Section 15.9 with any court as written evidence of the consent of the Purchaser and the Company to the waiver of the right to trial by jury.

15.10. Counterparts; Effectiveness. This Agreement may be executed in any number of counterparts and by different parties hereto in separate counterparts, with the same effect as if all parties had signed the same document. All such counterparts (including counterparts delivered by facsimile or other electronic format) shall be deemed an original, shall be construed together and shall constitute one and the same instrument. This Agreement shall become effective when each party hereto shall have received counterparts hereof signed by all of the other parties hereto.

15.11. Entire Agreement. The Transaction Documents contain the entire agreement among the parties hereto with respect to the subject matter hereof and thereof and such agreements supersede and replace all other prior agreements, written or oral, among the parties hereto with respect to the subject matter hereof and thereof.

15.12. Severability. If any provision of this Agreement shall be found by any court of competent jurisdiction to be invalid or unenforceable, the parties hereby waive such provision to the extent that it is found to be invalid or unenforceable. Such provision shall, to the maximum extent allowable by law, be modified by such court so that it becomes enforceable, and, as modified, shall be enforced as any other provision hereof, all the other provisions hereof continuing in full force and effect.

[Signature Pages Follow.]

IN WITNESS WHEREOF, the parties hereto have caused this Securities Purchase Agreement to be duly executed as of the day and year first written above.

THE COMPANY

A.P. PHARMA, INC.

By: /s/ John Whelan
Name: John Whelan
Title: Chief Executive Officer

[*Company Signature Page to Securities Purchase Agreement*]

IN WITNESS WHEREOF, the parties hereto have caused this Securities Purchase Agreement to be duly executed as of the day and year first written above.

THE PURCHASERS

TANG CAPITAL PARTNERS, LP

By: Tang Capital Management, LLC,
its general partner

By: /s Kevin Tang
Name: Kevin C. Tang
Title: Managing Director

BAKER BROS. INVESTMENTS II, L.P.

By: Baker Bros. Capital, L.P.,
its general partner
By: Baker Bros. Capital (GP), LLC,
its general partner

By: /s/ Felix Baker
Name: Felix Baker
Title: Managing Member

BAKER BROTHERS LIFE SCIENCES, L.P.

By: Baker Brothers Life Sciences Capital, L.P.,
its general partner
By: Baker Brothers Life Sciences Capital (GP), LLC, its
general partner

By: /s/ Felix Baker
Name: Felix Baker
Title: Managing Member

14159, L.P.

By: 14159 Capital, L.P., its general partner
By: 14159 Capital (GP), LLC, its general partner

By: /s/ Felix Baker
Name: Felix Baker
Title: Managing Member

EXHIBIT A

FORM OF SENIOR SECURED CONVERTIBLE NOTE DUE 2021

EXHIBIT B

FORM OF SECURITY AGREEMENT

SCHEDULE I

Name	Address	Initial Closing Investment Amount	Pro Rata Interest
Tang Capital Partners, LP	Tang Capital Partners, LP c/o Tang Capital Management, LLC 4401 Eastgate Mall San Diego, California 92121	$ 1,200,000	80%
Baker Bros. Investments II, L.P	Baker Bros. Investments II, L.P c/o Baker Brothers Investments 667 Madison Avenue, 21st Floor New York, NY 10065-8029	$ 300	0.02%
Baker Brothers Life Sciences, L.P.	Baker Brothers Life Sciences, L.P. c/o Baker Brothers Investments 667 Madison Avenue, 21st Floor New York, NY 10065-8029	$ 294,300	19.62%
14159, L.P.	14159, L.P. c/o Baker Brothers Investments 667 Madison Avenue, 21st Floor New York, NY 10065-8029	$ 5,400	0.36%

Exhibit 10.2

SENIOR SECURED CONVERTIBLE NOTE DUE 2021

NEITHER THE SECURITIES REPRESENTED BY THIS CERTIFICATE NOR THE SECURITIES INTO WHICH SUCH SECURITIES ARE CONVERTIBLE HAVE BEEN REGISTERED UNDER THE SECURITIES ACT OF 1933, AS AMENDED, OR APPLICABLE STATE SECURITIES LAWS. THE SECURITIES MAY NOT BE OFFERED FOR SALE, SOLD, TRANSFERRED OR ASSIGNED (I) IN THE ABSENCE OF (A) AN EFFECTIVE REGISTRATION STATEMENT FOR THE SECURITIES UNDER THE SECURITIES ACT OF 1933, AS AMENDED, OR (B) AN OPINION OF COUNSEL, IN A GENERALLY ACCEPTABLE FORM, THAT REGISTRATION IS NOT REQUIRED UNDER SAID ACT OR (II) UNLESS SOLD PURSUANT TO RULE 144 UNDER SAID ACT.

A.P. PHARMA, INC.

SENIOR SECURED CONVERTIBLE NOTE DUE 2021

Issuance Date: April [—], 2011 Principal: U.S. $_____

FOR VALUE RECEIVED, A.P. Pharma, Inc. a Delaware corporation (the "**Company**"), hereby promises to pay to _____or its registered assigns ("**Holder**") the amount set out above opposite the caption "**Principal**" (as such amount may be increased or reduced from time to time pursuant to the terms hereof, whether through the payment of PIK Interest (as defined below) or through redemption, conversion or otherwise, the "**Principal**") when due, whether upon the Maturity Date (as defined below), acceleration, redemption or otherwise (in each case, in accordance with the terms hereof) and to pay Interest (as defined below) on the outstanding Principal at the rates, in the manner and at the times set forth herein. This Senior Secured Convertible Note Due 2021 (including all Senior Secured Convertible Notes Due 2021 issued in exchange, transfer or replacement hereof, this "**Note**") is one of several Senior Secured Convertible Notes Due 2021 issued pursuant to the Securities Purchase Agreement (as defined below) (collectively, the "**Notes**" and such other Senior Secured Convertible Notes Due 2021, the "**Other Notes**"). Certain capitalized terms used herein are defined in Section 23. Capitalized terms used herein but not defined shall have the meaning given to such terms in the Securities Purchase Agreement.

(1) PAYMENTS OF PRINCIPAL. On the Maturity Date and upon the surrender of this Note, the Company shall pay to the Holder in cash, an amount equal to the outstanding Principal (if any) and accrued and unpaid Interest thereon. The "**Maturity Date**" shall be April [—], 2021, *provided* that the Holder may, upon providing ten (10) Business Days prior written notice, require prepayment of this Note at any time beginning on or after April [—], 2012. Other than as specifically permitted by this Note, the Company may not prepay any portion of the outstanding Principal or accrued and unpaid Interest, if any.

(2) INTEREST.

(a) Interest on this Note ("**Interest**") shall commence accruing at the Interest Rate on the Issuance Date and shall be computed on the basis of a 360-day year and twelve 30-day months and the actual number of days elapsed and shall be payable in arrears for each Calendar Quarter on the first day of the succeeding Calendar Quarter during the period beginning on the Issuance Date and ending on, and including, the Maturity Date (each, an "**Interest Date**") with the first Interest Date being July 1, 2011. Interest shall be payable on each Interest Date, to the record holder of this Note on the applicable Interest Date, through the addition of the amount of such Interest to the then outstanding Principal ("**PIK Interest**"); *provided however*, that for each Interest Date after October 1, 2011, the Holder may, at its option upon notice to the Company, elect to receive Interest on any Interest Date in cash ("**Cash Interest**") or in a combination of Cash Interest and PIK Interest. With respect to each Interest Date after October 1, 2011 for which the Holder elects to receive Cash Interest or a combination of Cash Interest and PIK Interest, the Holder shall deliver a written notice (each, an "**Interest Election Notice**") to the Company at least five (5) Business Days prior to the applicable Interest Date ("**Interest Notice Due Date**" and the date such notice is delivered to the Company, the "**Interest Notice Date**"), which notice elects to receive Interest as Cash Interest or a combination of Cash Interest and PIK Interest and specifies the amount of Interest that shall be paid as Cash Interest and the amount of Interest, if any, that shall be paid in PIK Interest. For the avoidance of doubt, if the Holder fails to deliver an Interest Election Notice on or prior to the Interest Notice Due Date, the Company shall pay the Holder PIK Interest on the applicable Interest Date. Interest that is paid in the form of PIK Interest shall be considered paid or duly provided for, for all purposes under this Note, and shall not be considered overdue.

(b) Accrued and unpaid Interest due on any portion of the Principal that is converted pursuant to Section 3 shall accrue through the Conversion Date and shall be paid on the next Interest Date, unless the entire outstanding Principal amount is being converted, in which case, the accrued and unpaid Interest shall be paid on the corresponding Share Delivery Date.

(3) CONVERSION OF NOTES. This Note shall be convertible into shares of the Company's common stock, par value $0.01 per share (the "**Common Stock**"), on the terms and conditions set forth in this Section 3.

(a) Conversion Right. Subject to the provisions of Section 3(d), at any time or times on or after the Issuance Date, the Holder shall be entitled to convert any portion of the outstanding and unpaid Conversion Amount (as defined below) into fully paid and non-assessable shares of Common Stock in accordance with Section 3(c), at the Conversion Rate (as defined below). The Company shall not issue any fraction of a share of Common Stock upon any conversion. If the issuance would result in the issuance of a fraction of a share of Common Stock, the Company shall round such fraction of a share of Common Stock up to the nearest whole share. The Company shall pay any and all transfer, stamp and similar taxes that may be payable with respect to the issuance and delivery of Common Stock upon conversion of any Conversion Amount.

(b) Conversion Rate. The number of shares of Common Stock issuable upon conversion of any Conversion Amount pursuant to Section 3(a) shall be determined by multiplying (x) such Conversion Amount by (y) the Conversion Rate (as defined below).

(i) "**Conversion Amount**" means the portion of the Principal to be converted, redeemed or otherwise with respect to which this determination is being made (which shall include PIK Interest, if applicable under Section 2(b)).

(ii) "**Conversion Rate**" means as of any Conversion Date (as defined below) or other date of determination during the period beginning on the Issuance Date and ending on and including the Maturity Date, 25,000 shares of Common Stock for every $1,000 of Conversion Amount.

(c) Mechanics of Conversion.

(i) Optional Conversion. To convert any Conversion Amount into shares of Common Stock on any date (a "**Conversion Date**"), the Holder shall (A) transmit by facsimile (or otherwise deliver), for receipt on or prior to 5:00 p.m., Pacific Time, on such date, a copy of an executed notice of conversion in the form attached hereto as Exhibit I (the "**Conversion Notice**") to the Company and (B) if required by Section 3(c)(iii), surrender this Note to a common carrier for delivery to the Company as soon as practicable on or following such date (or an indemnification undertaking with respect to this Note in the case of its loss, theft or destruction). On or before the first (1st) Business Day following the date of receipt of a Conversion Notice, the Company shall transmit by facsimile a confirmation of receipt of such Conversion Notice to the Holder and the Transfer Agent. On or before the third (3rd) Business Day following the date of receipt of a Conversion Notice (the "**Share Delivery Date**"), the Company shall issue and deliver to the address as specified in the Conversion Notice, a certificate, registered in the name of the Holder or its designee, for the number of shares of Common Stock to which the Holder shall be entitled, or, if requested by the Holder in the applicable Conversion Notice, the Company shall deliver the shares of Common Stock to which the Holder shall be entitled by Deposit/Withdrawal at Custodian ("**DWAC**") or other available means of electronic delivery through the Depository Trust Company. If this Note is physically surrendered for conversion as required by Section 3(c)(iii) and the outstanding Principal of this Note is greater than the portion of the Conversion Amount constituting principal, then the Company shall as soon as practicable and in no event later than three (3) Business Days after receipt of this Note (the "**Note Delivery Date**") and at its own expense, issue and deliver to the holder a new Note (in accordance with Section 13(d)) representing the outstanding Principal not converted. The Person or Persons entitled to receive the shares of Common Stock issuable upon a conversion of this Note shall be treated for all purposes as the record holder or holders of such shares of Common Stock on the Conversion Date to the extent permitted by applicable law.

(ii) Company's Failure to Timely Convert. If the Company shall fail to deliver via DWAC or issue a certificate to the Holder for the number of shares of Common Stock to which the Holder is entitled upon conversion of any Conversion Amount on or prior to the date which is three (3) Business Days after the Conversion Date (a "**Conversion Failure**"), then (A) the Company shall pay damages in cash to the Holder for each date of such Conversion Failure in an amount equal to 1.5% of the product of (I) the sum of the number of shares of Common Stock not issued to the Holder on or prior to the Share Delivery Date and to which the Holder is entitled, and (II) the Closing Sale Price of the Common Stock on the Share Delivery Date and (B) the Holder, upon written notice to the Company, may void its Conversion Notice with respect to, and retain or have returned, as the case may be, any portion of this Note that has not been converted pursuant to such Conversion Notice; provided that the voiding of a Conversion Notice shall not affect the Company's obligations to make any payments which have accrued prior to the date of such notice pursuant to this Section 3(c)(ii) or otherwise. At the Holder's option in lieu of the foregoing, if within three (3) Business Days after the Company's receipt of the facsimile copy of a Conversion Notice the Company shall fail to issue and deliver a certificate or shares via the DWAC system to the Holder for the number of shares of Common Stock to which the Holder is entitled upon such holder's conversion of any Conversion Amount, and if on or after such Trading Day the Holder purchases (in an open market transaction or otherwise) Common Stock to deliver in satisfaction of a sale by the Holder of Common Stock issuable upon such conversion that the Holder anticipated receiving from the Company (a "**Common Stock Buy-In**"), then the Company shall, within three (3) Business Days after the Holder's request (which shall include written evidence of a Common Stock Buy-In) and in the Holder's discretion, either (i) pay cash to the Holder in an amount equal to the Holder's total purchase price (including brokerage commissions, if any) for the shares of Common Stock so purchased (the "**Common Stock Buy-In Price**"), at which point the Company's obligation to deliver such certificate (and to issue such Common Stock) shall terminate, or (ii) promptly honor its obligation to deliver to the Holder a certificate or certificates representing such Common Stock and pay cash to the Holder in an amount equal to the excess (if any) of the Common Stock Buy-In Price over the product of (A) such number of shares of Common Stock, times (B) the Closing Bid Price on the Conversion Date.

(iii) Book-Entry. Notwithstanding anything to the contrary set forth herein, upon conversion of any portion of this Note in accordance with the terms hereof, the Holder shall not be required to physically surrender this Note to the Company unless (A) the full Principal represented by this Note is being converted, together with all accrued and unpaid Interest thereon, or (B) the Holder has provided the Company with prior written notice (which notice may be included in a Conversion Notice) requesting reissuance of this Note upon physical surrender of this Note. The Holder and the Company shall maintain records showing the portion of Principal and Interest converted and the dates of such conversions or

shall use such other method, reasonably satisfactory to the Holder and the Company, so as not to require physical surrender of this Note upon conversion.

(iv) Pro Rata Conversion; Disputes. In the event that the Company receives a Conversion Notice from more than one holder of Notes for the same Conversion Date and the Company can convert some, but not all, of such portions of the Notes submitted for conversion, the Company shall convert from each holder of Notes electing to have a portion of its Notes converted on such date a pro rata amount of such holder's portion of its Notes submitted for conversion based on the principal portion submitted for conversion on such date by such holder relative to the aggregate principal portions of all Notes submitted for conversion on such date. In the event of a dispute as to the number of shares of Common Stock issuable to the Holder in connection with a conversion of this Note, the Company shall issue to the Holder the number of shares of Common Stock not in dispute and resolve such dispute in accordance with Section 18.

(d) Limitations on Conversions.

(i) Beneficial Ownership. The Company shall not effect any conversion of this Note, and the Holder of this Note shall not have the right to convert any portion of this Note pursuant to Section 3(a), to the extent that after giving effect to such conversion, the Holder (together with the Holder's affiliates) would beneficially own in excess of 9.99% (subject to change as described below, the "**Maximum Percentage**") of the number of shares of Common Stock outstanding immediately after giving effect to such conversion. For purposes of the foregoing sentence, the number of shares of Common Stock beneficially owned by the Holder and its affiliates shall include the number of shares of Common Stock issuable upon conversion of this Note with respect to which the determination of such sentence is being made, but shall exclude the number of shares of Common Stock which would be issuable upon (A) conversion of the remaining, non-converted portion of this Note beneficially owned by the Holder or any of its affiliates and (B) exercise or conversion of the unexercised or non-converted portion of any other securities of the Company (including, without limitation, any Other Notes or warrants) subject to a limitation on conversion or exercise analogous to the limitation contained herein beneficially owned by the Holder or any of its affiliates. Except as set forth in the preceding sentence, for purposes of this Section 3(d)(i), beneficial ownership shall be calculated in accordance with Section 13(d) of the Securities Exchange Act of 1934, as amended (the "**1934 Act**"). For purposes of this Section 3(d)(i), in determining the number of outstanding shares of Common Stock, the Holder may rely on the number of outstanding shares of Common Stock as reflected in (x) the Company's most recent Form 10-K, Form 10-Q, Form 8-K or other public filing with the Securities Exchange Commission, as the case may be, (y) a more recent public announcement by the Company or (z) any other notice by the Company or the Transfer Agent setting forth the number of shares of Common Stock outstanding. For any reason at any time, upon the written or oral request of the Holder, the

Company shall within one (1) Business Day confirm orally and in writing to the Holder the number of shares of Common Stock then outstanding. In any case, the number of outstanding shares of Common Stock shall be determined after giving effect to the conversion or exercise of securities of the Company, including this Note, by the Holder or its affiliates since the date as of which such number of outstanding shares of Common Stock was reported. By written notice to the Company, the Holder may increase or decrease the Maximum Percentage to any other percentage; provided that (i) any such increase or decrease will not be effective until the sixty-first (61st) day after such notice is delivered to the Company, and (ii) any such increase or decrease will apply only to the Holder and not to any other holder of Notes.

(4) EVENTS OF DEFAULT; RIGHTS UPON EVENT OF DEFAULT.

(a) Events of Default. Each of the following events (so long as it is continuing) shall constitute an "**Event of Default**":

(i) the Company's (A) failure to cure a Conversion Failure with respect to any of the Notes by delivery of the required number of shares of Common Stock within ten (10) Business Days after the applicable Conversion Date or (B) notice, written or oral, to any holder of the Notes, including by way of public announcement or through any of its agents, at any time, of its intention not to comply with a request for conversion of any Notes into shares of Common Stock that is tendered for conversion in compliance with the provisions of the Notes and applicable securities laws;

(ii) the Company's failure to pay to any Holder any amount of Principal, premium (if any), Interest, or other amounts when and as due under this Note (including, without limitation, the Company's failure to pay any redemption payments hereunder), any other Transaction Document or any other agreement, document, certificate or other instrument delivered in connection with the transactions contemplated hereby and thereby to which such Holder is a party, provided, that in the case of a failure to pay Interest when and as due, such failure shall constitute an Event of Default only if such failure continues for a period of at least five (5) Business Days;

(iii) any event of default under, redemption of or acceleration prior to maturity of any Indebtedness of the Company, other than the Notes, in an aggregate principal amount in excess of $100,000;

(iv) any default under a Material Contract;

(v) the Company, pursuant to or within the meaning of Title 11, U.S. Code, or any similar Federal, foreign or state law for the relief of debtors (collectively, "**Bankruptcy Law**"), (A) commences a voluntary case, (B) consents to the entry of an order for relief against it in an involuntary case, (C) consents to the

appointment of a receiver, trustee, assignee, liquidator or similar official (a "**Custodian**"), (D) makes a general assignment for the benefit of its creditors, or (E) admits in writing that it is generally unable to pay its debts as they become due;

(vi) a court of competent jurisdiction enters an order or decree under any Bankruptcy Law that (A) is for relief against the Company in an involuntary case, (B) appoints a Custodian of the Company or (C) orders the liquidation of the Company;

(vii) a final judgment or judgments for the payment of money aggregating in excess of $100,000 are rendered against the Company and which judgments are not, within sixty (60) days after the entry thereof, bonded, discharged or stayed pending appeal, or are not discharged within sixty (60) days after the expiration of such stay; provided, however, that any judgment which is covered by insurance or an indemnity from a creditworthy party shall not be included in calculating the $100,000 amount set forth above so long as the Company provides the Holder with a written statement from such insurer or indemnity provider (which written statement shall be reasonably satisfactory to the Holder) to the effect that such judgment is covered by insurance or an indemnity and the Company will receive the proceeds of such insurance or indemnity within thirty (30) days of the issuance of such judgment or such later date as provided by the terms of such insurance policy;

(viii) any representation or warranty made by the Company in any Transaction Document shall prove to be materially false or misleading as of the date made or deemed made;

(ix) the Company shall breach any covenant or other term or condition of any Transaction Document and, in the case of a breach of a covenant or term or condition which is curable, such breach continues for a period of at least ten (10) consecutive Business Days;

(x) any material provision of any Transaction Document ceases to be of full force and effect other than by its terms, or the Company contests in writing (or supports any other person in contesting) the validity or enforceability of any provision of any Transaction Document;

(xi) the Security Agreement shall for any reason (other than pursuant to the terms thereof) cease to create a valid and perfected lien, with the priority required by the Security Agreement, on, and security interest in, any material portion of the Collateral purported to be covered thereby, subject to Permitted Liens;

(xii) the failure of the applicable Registration Statement required to be filed pursuant to the Securities Purchase Agreement to be declared effective by the Commission on or prior to the date that is sixty (60) days after the applicable Effectiveness

Deadline (as defined in the Securities Purchase Agreement), or, while the applicable Registration Statement is required to be maintained effective pursuant to the terms of the Securities Purchase Agreement, the effectiveness of the applicable Registration Statement lapses for any reason (including, without limitation, the issuance of a stop order) or is unavailable to any holder of the Notes for sale of all of such holder's Registrable Securities (as defined in the Securities Purchase Agreement) in accordance with the terms of the Securities Purchase Agreement, and such lapse or unavailability continues for a period of twenty (20) consecutive days or for more than an aggregate of forty-five (45) days in any 365-day period (other than days during an Allowable Grace Period (as defined in the Securities Purchase Agreement)); or

(xiii) any breach or failure in any respect to comply with Section 11 of this Note.

(b) Redemption Right. Upon the occurrence of an Event of Default with respect to this Note, the Company, within two (2) Business Days of the date on which the Company becomes aware of or reasonably should have become aware of such Event of Default, shall deliver written notice thereof via facsimile and overnight courier (an "**Event of Default Notice**") to the Holder. At any time after the earlier of the Holder's receipt of an Event of Default Notice and the Holder becoming aware of an Event of Default, the Holder may require the Company to redeem all or any portion of this Note by delivering written notice thereof (the "**Event of Default Redemption Notice**") to the Company, which Event of Default Redemption Notice shall indicate the Conversion Amount of this Note the Holder is electing to require the Company to redeem. Each portion of this Note subject to redemption by the Company pursuant to this Section 4(b) shall be redeemed by the Company at a price equal to the greater of the following two formulas (such greater price being referred to herein as the "**Event of Default Redemption Price**"): (i) A = B * C; or (ii) A = (B * D) * E.

Where:

A	=	Amount due to the Holder on redemption pursuant to Section 4(b);
B	=	Conversion Amount to be redeemed, together with any accrued and unpaid Interest, if any, on such Conversion Amount and Interest through the redemption date;
C	=	The Redemption Multiplier;
D	=	The Conversion Rate with respect to such Conversion Amount in effect at such time as the Holder delivers an Event of Default Redemption Notice; and
E	=	The greatest of: (1) the Closing Sale Price of the Common Stock on the date immediately preceding such Event of Default, (2) the Closing Sale Price of the Common Stock on the date immediately after such Event of Default, and (3) the Closing Sale Price of the

Common Stock on the date the Holder delivers the Event of Default Redemption Notice.

Redemptions required by this Section 4(b) shall be made in accordance with the provisions of Section 9. To the extent redemptions required by this Section 4(b) are deemed or determined by a court of competent jurisdiction to be prepayments of the Note by the Company, such redemptions shall be deemed to be voluntary prepayments. The parties hereto agree that in the event of the Company's redemption of any portion of the Note under this Section 4(b), the Holder's damages would be uncertain and difficult to estimate because of the parties' inability to predict future interest rates and the uncertainty of the availability of a suitable substitute investment opportunity for the Holder. Accordingly, any amount due under this Section 4(b) is intended by the parties to be, and shall be deemed, a reasonable estimate of the Holder's actual loss of its investment opportunity and not as a penalty.

(5) RIGHTS UPON CHANGE OF CONTROL.

(a) Assumption. The Company shall not enter into or be party to a Change of Control unless (i) the Successor Entity assumes in writing all of the obligations of the Company under this Note and the other Transaction Documents in accordance with the provisions of this Section 5(a) pursuant to written agreements in form and substance satisfactory to the Required Holders and approved by the Required Holders (such approval not to be unreasonably withheld or delayed) prior to such Change of Control, including agreements to deliver to each holder of Notes in exchange for such Notes a security of the Successor Entity evidenced by a written instrument substantially similar in form and substance to the Notes, including, without limitation, having a principal amount and interest rate equal to the principal amounts and the interest rates of the Notes held by such holder and having similar ranking to the Notes, and satisfactory to the Required Holders (any such approval not to be unreasonably withheld or delayed) and (ii) the Successor Entity (including its Parent Entity) is a publicly traded corporation whose common stock is quoted on or listed for trading on an Eligible Market. Upon the occurrence of any Change of Control, the Successor Entity shall succeed to, and be substituted for (so that from and after the date of such Change of Control, the provisions of this Note referring to the "Company" shall refer instead to the Successor Entity), and may exercise every right and power of the Company and shall assume all of the obligations of the Company under this Note with the same effect as if such Successor Entity had been named as the Company herein. Upon consummation of the Change of Control, the Successor Entity shall deliver to the Holder confirmation that there shall be issued upon conversion or redemption of this Note at any time after the consummation of the Change of Control, in lieu of the shares of the Common Stock (or other securities, cash, assets or other property) purchasable upon the conversion or redemption of the Notes prior to such Change of Control, such shares of stock, securities, cash, assets or any other property whatsoever (including warrants or other purchase or subscription rights) which the Holder would have been entitled to receive upon the consummation of such Change of Control had this Note been converted immediately prior to such Change of Control, as adjusted in accordance with the provisions of this Note. The provisions of this Section shall apply similarly and equally to successive Change of Controls and shall be applied without regard to any limitations on the conversion or redemption of this Note.

(b) Holder Redemption Right. No later than ten (10) days prior to the consummation of a Change of Control, the Company shall deliver written notice thereof via facsimile and overnight courier to the Holder (a "**Change of Control Notice**"). At any time during the period beginning after the Holder's receipt of a Change of Control Notice and ending on the date of the consummation of such Change of Control (or, in the event a Change of Control Notice is not delivered at least ten (10) days prior to a Change of Control, at any time on or after the date which is ten (10) days prior to a Change of Control and ending ten (10) days after the consummation of such Change of Control), the Holder may require the Company to redeem all or any portion of this Note in cash by delivering written notice thereof ("**Change of Control Redemption Notice**") to the Company, which Change of Control Redemption Notice shall indicate the Conversion Amount the Holder is electing to redeem. The portion of this Note subject to redemption pursuant to this Section 5 shall be redeemed by the Company at a price equal to the product of (x) the Conversion Amount being redeemed, together with any accrued and unpaid Interest, if any, on such Conversion Amount and Interest through the redemption date, and (y) the Redemption Multiplier (the "**Change of Control Redemption Price**"). Redemptions required by this Section 5(b) shall be made in accordance with the provisions of Section 9 and shall have priority to payments to common stockholders in connection with a Change of Control. Notwithstanding anything to the contrary in this Section 5(b), until the Change of Control Redemption Price (together with any interest thereon) is paid in full, the Conversion Amount and any Interest submitted for redemption under this Section 5(b) (together with any interest thereon) may be converted, in whole or in part, by the Holder into Common Stock pursuant to Section 3.

(6) RIGHTS UPON ISSUANCE OF PURCHASE RIGHTS AND OTHER CORPORATE EVENTS.

(a) Purchase Rights. If at any time the Company grants, issues or sells any Options, Convertible Securities or rights to purchase stock, warrants, securities or other property pro rata to the record holders of any class of Common Stock (the "**Purchase Rights**"), then the Holder will be entitled to acquire, upon the terms applicable to such Purchase Rights, the aggregate Purchase Rights which the Holder could have acquired if the Holder had held the number of shares of Common Stock acquirable upon complete conversion of this Note (without taking into account any limitations or restrictions on the convertibility of this Note) immediately before the date on which a record is taken for the grant, issuance or sale of such Purchase Rights, or, if no such record is taken, the date as of which the record holders of Common Stock are to be determined for the grant, issue or sale of such Purchase Rights.

(b) Other Corporate Events. Subject to Section 6(a) hereof, in addition to and not in substitution for any other rights hereunder, prior to the consummation of any Change of Control pursuant to which holders of shares of Common Stock are entitled to receive securities or other assets with respect to or in exchange for shares of Common Stock (a "**Corporate Event**"), the Company shall make appropriate provision to ensure that the Holder will thereafter have the right to receive upon a conversion of this Note, (i) in addition to the shares of Common Stock receivable upon such conversion, such securities or other assets to which the Holder would have been entitled with respect to such shares of Common

Stock had such shares of Common Stock been held by the Holder upon the consummation of such Corporate Event (without taking into account any limitations or restrictions on the convertibility of this Note), or (ii) in lieu of the shares of Common Stock otherwise receivable upon such conversion, such securities or other assets received by the holders of shares of Common Stock in connection with the consummation of such Corporate Event in such amounts as the Holder would have been entitled to receive had this Note initially been issued with conversion rights for the form of such consideration (as opposed to shares of Common Stock) at a conversion rate for such consideration commensurate with the Conversion Rate. Provision made pursuant to the preceding sentence shall be in a form and substance satisfactory to the Holder. The provisions of this Section shall apply similarly and equally to successive Corporate Events and shall be applied without regard to any limitations on the conversion or redemption of this Note.

(7) RIGHTS UPON ISSUANCE OF OTHER SECURITIES.

(a) Pro Rata Distributions. If the Company, at any time while this Note is outstanding, distributes to all holders of Common Stock (i) evidences of its Indebtedness, (ii) any security (other than a distribution of Common Stock covered by the preceding paragraph), (iii) rights or warrants to subscribe for or purchase any security, or (iv) any other asset (in each case "**Distributed Property**"), then, unless taken into account pursuant to Section 7(b) below, upon any conversion of this Note that occurs after such record date, the Holder shall be entitled to receive, in addition to the shares of Common Stock otherwise issuable upon such conversion, the Distributed Property that the Holder would have been entitled to receive in respect of such number of shares of Common Stock immediately prior to such record date.

(b) Adjustment of Conversion Rate upon Subdivision or Combination of Common Stock. If the Company at any time on or after the Subscription Date subdivides (by any stock split, stock dividend, recapitalization or otherwise) one or more classes of its outstanding shares of Common Stock into a greater number of shares, the Conversion Rate in effect immediately prior to such subdivision will be proportionately increased. If the Company at any time on or after the Subscription Date combines (by combination, reverse stock split or otherwise) one or more classes of its outstanding shares of Common Stock into a smaller number of shares, the Conversion Rate in effect immediately prior to such combination will be proportionately decreased.

(8) NONCIRCUMVENTION. The Company hereby covenants and agrees that the Company will not, by amendment of its Certificate of Incorporation, Bylaws or through any reorganization, transfer of assets, consolidation, merger, scheme of arrangement, dissolution, issue or sale of securities, or any other voluntary action, avoid or seek to avoid the observance or performance of any of the terms of this Note, and will at all times in good faith carry out all of the provisions of this Note and take all action as may be required to protect the rights of the Holder of this Note.

(9) HOLDER'S REDEMPTIONS.

(a) If the Holder has submitted an Event of Default Redemption Notice in accordance with Section 4(b), then the Company shall deliver the Event of Default Redemption Price to the Holder within five (5) Business Days after the delivery of the Event of Default Redemption Notice.

(b) If the Holder has submitted a Change of Control Redemption Notice in accordance with Section 5(b), then the Company shall deliver the Change of Control Redemption Price to the Holder concurrently with the consummation of such Change of Control if such notice is delivered to the Company at least five (5) Business Days prior to the consummation of such Change of Control. If the Change of Control Redemption Notice is delivered to the Company less than five (5) Business Days prior to the consummation of such Change of Control, then the Change of Control Redemption Price shall be delivered no more than five (5) Business Days after the delivery of the Change of Control Redemption Notice.

(c) In the event of a redemption of less than all of the Principal of this Note under Sections 4(b) or 5(b), the Company shall promptly cause to be issued and delivered to the Holder (after such original Note has been delivered to the Company) a new Note representing the outstanding Principal that has not been redeemed. In the event that the Company does not pay the required redemption amount to the Holder within the time periods required under Section 9(a) or 9(b), as applicable, at any time thereafter and until the Company pays such amount in full, the Holder shall have the option, in lieu of redemption, to require the Company to promptly return to the Holder all or any portion of this Note representing the Conversion Amount that was submitted for redemption and for which the redemption amount has not been paid. Upon the Company's receipt of such notice, (x) the redemption notice shall be null and void with respect to such Conversion Amount and (y) the Company shall immediately return this Note, or issue a new Note to the Holder representing such Conversion Amount.

(d) Redemption by Other Holders. Upon the Company's receipt of notice from any of the holders of the Other Notes for redemption or repayment as a result of an event or occurrence substantially similar to the events or occurrences described in Sections 5(b) (each, an "**Other Redemption Notice**"), the Company shall immediately forward to the Holder by facsimile a copy of such notice. If the Company timely receives a Change of Control Redemption Notice and one or more Other Redemption Notices and the Company is unable to redeem all Principal, Interest and other amounts designated in such Change of Control Redemption Notice and such Other Redemption Notices, then the Company shall redeem a pro rata amount from each holder of the Notes (including the Holder) based on the Principal amounts of the Notes submitted for redemption pursuant to such Change of Control Redemption Notice and pursuant to such Other Redemption Notices received by the Company.

(10) RIGHTS. Except as otherwise provided for herein, the Holder shall have no rights as a stockholder of the Company as a result of being a holder of this Note, except as

required by law, including, but not limited to, the General Corporation Law of the State of Delaware, and as expressly provided in this Note.

(11) COVENANTS.

(a) Rank. All payments due under this Note (a) shall rank *pari passu* with all Other Notes and (b) shall be senior to all other Indebtedness of the Company.

(b) Incurrence of Indebtedness. So long as this Note is outstanding, the Company shall not, and the Company shall not directly or indirectly, incur or guarantee, assume or suffer to exist any Indebtedness, other than Permitted Indebtedness.

(c) Existence of Liens. So long as this Note is outstanding, the Company shall not, and the Company shall not permit any of its Subsidiaries to, directly or indirectly, allow or suffer to exist any mortgage, lien, pledge, charge, security interest or other similar encumbrance upon or in any property or assets (including accounts and contract rights) owned by the Company or any of its Subsidiaries (collectively "**Liens**") other than Permitted Liens.

(d) Restricted Payments. The Company shall not, and the Company shall not permit any of its Subsidiaries to, directly or indirectly, redeem, defease, repurchase, repay or make any payments in respect of, by the payment of cash or cash equivalents (in whole or in part, whether by way of open market purchases, tender offers, private transactions or otherwise), all or any portion of any Indebtedness described in clause (2) of the definition of "Permitted Indebtedness", whether by way of payment in respect of principal of (or premium, if any) or interest on such Indebtedness if at the time such payment is due or is otherwise made or, after giving effect to such payment, an event constituting, or that with the passage of time and without being cured would constitute, an Event of Default has occurred and is continuing.

(e) Transactions with Affiliates. The Company shall not directly or indirectly enter into or permit to exist any transaction with any Affiliate except for (i) transactions (other than the payment of management, consulting, monitoring or advisory fees) between the Company, on the one hand, and any Affiliate of the Company, on the other hand, so long as such transactions are (x) upon fair and reasonable terms and (y) are fully disclosed to Holder if they involve one or more payments by the Company in excess of $100,000 for any single transaction or series of transactions, (ii) the payment of reasonable fees, compensation, or employee benefit arrangements to outside directors and executive officers and any indemnity provided for the benefit of directors, of Company in the ordinary course of business, or (iii) in connection with the Secured Obligations.

(f) Disposition of Assets. The Company shall not convey, sell, lease, license, assign, transfer or otherwise dispose of (or enter into an agreement to convey, sell, lease, license, assign, transfer, or otherwise dispose of) any of the Company's assets other than (i) sales or other dispositions of equipment that is substantially worn, damaged or obsolete in the ordinary course of business, (ii) sales or leases of inventory to buyers or lessees in the

ordinary course of business, (iii) the use or transfer of cash in a manner that is not prohibited by the terms of the Transaction Documents, (iv) the licensing, on a non-exclusive basis, of patents, trademarks, copyrights, and other intellectual property rights in the ordinary course of business, and (v) other sales and dispositions of assets with an aggregate value not exceeding $100,000 in any fiscal year; *provided*, that the aggregate amount of sales of Equipment pursuant to clauses (i), (ii) and (v) above may not exceed $250,000 in the aggregate in any fiscal year.

(g) Investments. Except for Permitted Investments, the Company shall not directly or indirectly, make or acquire any investment or incur any Liabilities (including Contingent Obligations) for or in connection with any investment; *provided, however*, that the Company shall not, starting 30 days after the Effective Date, have Permitted Investments in Deposit Accounts or Securities Accounts unless the Company and the applicable securities intermediary or bank have entered into control agreements governing such Permitted Investments in order to perfect (and further establish) the Liens in such Permitted Investments.

(h) Material Contracts. The Company shall not directly or indirectly, amend, modify, alter, increase, or change any of the terms or conditions of (i) any agreement, instrument, document, indenture, or other writing evidencing or concerning Indebtedness permitted under Section 11(b), (ii) any Charter Documents, or (iii) any Material Contract except to the extent that such amendment, modification, alteration, increase, or change to such Material Contract could not, individually or in the aggregate, reasonably be expected to result in a Material Adverse Effect.

(12) VOTE TO AMEND NOTES. The affirmative vote at a meeting duly called for such purpose or the written consent without a meeting of the Required Holders shall be required for any change or amendment to this Note or the Other Notes.

(13) REISSUANCE OF THIS NOTE.

(a) Transfer. If this Note is to be transferred in compliance with the Securities Purchase Agreement, the Holder shall surrender this Note to the Company, whereupon the Company will forthwith issue and deliver upon the order of the Holder a new Note, registered as the Holder may request, representing the outstanding Principal being transferred by the Holder and, if less then the entire outstanding Principal is being transferred, a new Note to the Holder representing the outstanding Principal not being transferred. The Holder and any assignee, by acceptance of this Note, acknowledge and agree that, by reason of the provisions of Section 3(c)(iii), following conversion or redemption of any portion of this Note, the outstanding Principal represented by this Note may be less than the Principal stated on the face of this Note.

(b) Lost, Stolen or Mutilated Note. Upon receipt by the Company of evidence reasonably satisfactory to the Company of the loss, theft, destruction or mutilation of this Note, and, in the case of loss, theft or destruction, of an indemnification undertaking by the Holder to the Company, in customary form and, in the case of mutilation, upon surrender and

cancellation of this Note, the Company shall execute and deliver to the Holder a new Note representing the outstanding Principal.

(c) Note Exchangeable for Different Denominations. This Note is exchangeable, upon the surrender hereof by the Holder at the principal office of the Company, for a new Note or Notes representing in the aggregate the outstanding Principal of this Note, and each such new Note will represent such portion of such outstanding Principal as is designated by the Holder at the time of such surrender.

(d) Issuance of New Notes. Whenever the Company is required to issue a new Note pursuant to the terms of this Note, such new Note (i) shall be of like tenor with this Note, (ii) shall represent, as indicated on the face of such new Note, the Principal remaining outstanding, (iii) shall have an issuance date, as indicated on the face of such new Note which is the same as the Issuance Date of this Note, (iv) shall have the same rights and conditions as this Note, and (v) shall represent accrued and unpaid Interest of this Note from the Issuance Date.

(14) REMEDIES, CHARACTERIZATIONS, OTHER OBLIGATIONS, BREACHES AND INJUNCTIVE RELIEF.

(a) The remedies provided in this Note shall be cumulative and in addition to all other remedies available under this Note and any of the other Transaction Documents, at law or in equity (including a decree of specific performance and/or other injunctive relief), and nothing herein shall limit the Holder's right to pursue monetary damages for any failure by the Company to comply with the terms of this Note. Amounts set forth or provided for herein with respect to payments, conversion and the like (and the computation thereof) shall be the amounts to be received by the Holder and shall not, except as expressly provided herein, be subject to any other obligation of the Company (or the performance thereof). The Company acknowledges that a breach by it of its obligations hereunder will cause irreparable harm to the Holder and that the remedy at law for any such breach may be inadequate. The Company therefore agrees that, in the event of any such breach or threatened breach, the Holder shall be entitled, in addition to all other available remedies, to an injunction restraining any breach, without the necessity of showing economic loss and without any bond or other security being required.

(b) Notwithstanding the foregoing, the right of the Holder to receive payment of Principal, premium, if any, and Interest on the Note, on or after the respective due dates set forth herein (including in connection with a Change of Control), or convert any portion of the Note into shares of Common Stock on the terms and conditions set forth herein, or to bring suit for the enforcement of any such right to payment or conversion, shall not be impaired or affected without the consent of the Holder.

(15) PAYMENT OF COLLECTION, ENFORCEMENT AND OTHER COSTS. If (a) this Note is placed in the hands of an attorney for collection or enforcement or is collected or enforced through any legal proceeding or the Holder otherwise takes action to collect amounts due under this Note or to enforce the provisions of this Note or (b) there occurs any bankruptcy,

reorganization, receivership of the Company or other proceedings affecting Company creditors' rights and involving a claim under this Note, then the Company shall pay the costs incurred by the Holder for such collection, enforcement or action or in connection with such bankruptcy, reorganization, receivership or other proceeding, including, but not limited to, reasonable attorneys' fees and disbursements.

(16) CONSTRUCTION; HEADINGS. This Note shall be deemed to be jointly drafted by the Company and the Purchaser and shall not be construed against any person as the drafter hereof. The headings of this Note are for convenience of reference and shall not form part of, or affect the interpretation of, this Note.

(17) FAILURE OR INDULGENCE NOT WAIVER. No failure or delay on the part of the Holder in the exercise of any power, right or privilege hereunder shall operate as a waiver thereof, nor shall any single or partial exercise of any such power, right or privilege preclude other or further exercise thereof or of any other right, power or privilege.

(18) DISPUTE RESOLUTION. In the case of a dispute as to the determination of the Closing Bid Price, the Closing Sale Price, the Redemption Price or the arithmetic calculation of the Conversion Rate or the Redemption Price, the Company shall submit the disputed determinations or arithmetic calculations via facsimile within one (1) Business Day of receipt, or deemed receipt, of the Conversion Notice or the Change of Control Redemption Notice or other event giving rise to such dispute, as the case may be, to the Holder. If the Holder and the Company are unable to agree upon such determination or calculation of the Redemption Price or the Conversion Rate, as applicable, within one (1) Business Day of such disputed determination or arithmetic calculation being submitted to the Holder, then the Company and the Holder shall, within one (1) Business Day thereafter submit via facsimile (a) the disputed determination of the Closing Bid Price, the Closing Sale Price, to an independent, reputable investment bank selected by the Company and approved by the Holder or (b) the disputed arithmetic calculation of the Conversion Rate or the Redemption Price to the Company's independent, outside accountant. The Company, at the Company's expense, shall cause the investment bank or the accountant, as the case may be, to perform the determinations or calculations and notify the Company and the Holder of the results no later than five (5) Business Days from the time it receives the disputed determinations or calculations. Such investment bank's or accountant's determination or calculation, as the case may be, shall be binding upon all parties absent manifest error.

(19) NOTICES; PAYMENTS.

(a) Notices. Whenever notice is required to be given under this Note, unless otherwise provided herein, such notice shall be given in accordance with Section 15.2 of the Securities Purchase Agreement. The Company shall provide the Holder with prompt written notice of all actions taken pursuant to this Note, including in reasonable detail a description of such action and the reason therefore. Without limiting the generality of the foregoing, the Company will give written notice to the Holder (i) within one (1) Business Day upon any adjustment of the Conversion Rate, setting forth in reasonable detail, and certifying, the calculation of such adjustment and (ii) at least fifteen (15) days prior to the date on which the Company closes its books or takes a record (A) with respect to any dividend or distribution

upon the Common Stock, (B) with respect to any pro rata subscription offer to holders of Common Stock or (C) for determining rights to vote with respect to any Change of Control, dissolution or liquidation, provided in each case that such information shall be made known to the public prior to or in conjunction with such notice being provided to the Holder.

(b) Payments. Whenever any payment of cash is to be made by the Company to any Person pursuant to this Note, such payment shall be made in lawful money of the United States of America by a check drawn on the account of the Company and sent via overnight courier service to such Person at such address as previously provided to the Company in writing (which address, in the case of each of the Purchasers shall initially be as set forth in Section 15.2 of the Securities Purchase Agreement); provided that the Holder may elect to receive a payment of cash via wire transfer of immediately available funds by providing the Company with prior written notice setting out such request and the Holder's wire transfer instructions. Whenever any amount expressed to be due by the terms of this Note is due on any day which is not a Business Day, the same shall instead be due on the next succeeding day which is a Business Day.

(c) Withholding Taxes. All payments made by the Company hereunder shall be made without withholding for or on account of any present or future taxes (other than overall net income taxes imposed on the recipient). If any such withholding is so required, the Company shall make the withholding, pay the amount withheld to the appropriate authority before penalties attach thereto or interest accrues thereon and pay to the recipient such additional amount as may be necessary to ensure that the net amount actually received by the recipient free and clear of such taxes (including taxes on such additional amount) is equal to the amount that the recipient would have received had such withholding not been made. If the recipient is required to pay any such taxes, penalties or interest, the Company shall reimburse the recipient for that payment on demand. If the Company pays any such taxes, penalties or interest, it shall deliver official tax receipts or other evidence of payment to the recipient on whose account such withholding was made on or before the thirtieth day after payment. The Holder agrees to provide, promptly following the Company's request therefore, such forms or certifications as it is legally able to provide to establish an exemption from, or a reduction in, any withholding taxes that might otherwise apply.

(20) CANCELLATION. After all Principal, accrued Interest and other amounts at any time owed on this Note have been paid in full, this Note shall automatically be deemed canceled, shall be surrendered to the Company for cancellation and shall not be reissued.

(21) WAIVER OF NOTICE. To the extent permitted by law, the Company hereby waives demand, notice, protest and all other demands and notices in connection with the delivery, acceptance, performance, default or enforcement of this Note and the Securities Purchase Agreement.

(22) GOVERNING LAW. This Note shall be construed and enforced in accordance with, and all questions concerning the construction, validity, interpretation and performance of this Note shall be governed by, the internal laws of the State of California, without giving effect to any choice of law or conflict of law provision or rule (whether of the State of California or any

other jurisdictions) that would cause the application of the laws of any jurisdictions other than the State of California.

(23) CERTAIN DEFINITIONS. For purposes of this Note, the following terms shall have the following meanings:

(a) "**Bankruptcy Code**" means Chapter 11 of Title 11 of the United States Code, as amended from time to time and any successor statute and all rules and regulations promulgated thereunder.

(b) "**Bankruptcy Law**" has the meaning assigned to it in Section 4(a)(iv) hereof.

(c) "**Beneficial Ownership**" has the meaning set forth in Rule 13d-3 under the Exchange Act.

(d) "**Bloomberg**" means Bloomberg Financial Markets.

(e) **"Board of Directors**" means the board of directors of the Company or any authorized committee of the board of directors.

(f) "**Business Day**" means any day other than Saturday, Sunday or other day on which commercial banks in the City of New York are authorized or required by law to remain closed.

(g) "**Calendar Quarter**" means each of the period beginning on and including January 1 and ending on and including March 31; the period beginning on and including April 1 and ending on and including June 30; the period beginning on and including July 1 and ending on and including September 30; and the period beginning on and including October 1 and ending on and including December 31.

(h) "**Cash Interest**" has the meaning assigned to it in Section 2 hereof.

(i) "**Company**" has the meaning assigned to it in the introduction hereof.

(j) "**Contractual Obligation**" means, with respect to any Person, any contract, agreement, deed, mortgage, lease, sublease, license, sublicense or other legally enforceable commitment, promise, undertaking, obligation, arrangement, instrument or understanding, whether written or oral, to which or by which such Person is a party or otherwise subject or bound or to which or by which any property, business, operation or right of such Person is subject or bound.

(k) "**Change of Control**" means: (1) the Company shall, directly or indirectly, in one or more related transactions consolidate or merge with or into (whether or not the Company is the surviving corporation) a Person or Persons, or (2) that the Company shall, directly or indirectly, in one or more related transactions sell, assign, transfer, license, convey or otherwise dispose of all or substantially all of the assets of the Company to a

Person or Persons (for the avoidance of doubt, the sale, assignment, transfer, license, conveyance or other disposition of the Company's rights to the compound designated "APF530" shall be deemed a sale of "substantially all" of the Company's assets), or (3) a Person or Persons acting in concert to make a purchase, tender or exchange offer that is accepted by the holders of more than the 50% of the outstanding shares of Common Stock (not including any shares of Common Stock held by the Person or Persons making or party to, or associated or affiliated with the Persons making or party to, such purchase, tender or exchange offer), or (4) the Company shall, directly or indirectly, in one or more related transactions consummate a securities purchase agreement or business combination (including, without limitation, a reorganization, recapitalization, spin-off) with a Person or Persons, in one or more related transactions, whereby such Person(s) acquire Beneficial Ownership (without regard to any conversion limitations or delays on the securities convertible into Common Stock, if any) of more than 50% of the number of shares of Common Stock issued and outstanding as of one Business Day prior to the Initial Closing, or (5) reorganize, recapitalize or reclassify its Common Stock.

(l) "**Change of Control Notice**" has the meaning assigned to it in Section 5(b) hereof.

(m) "**Change of Control Redemption Notice**" has the meaning assigned to it in Section 5(b) hereof.

(n) "**Change of Control Redemption Price**" has the meaning assigned to it in Section 5(b) hereof.

(o) "**Charter Documents**" means the certificate of incorporation and by-laws of the Company.

(p) "**Closing Bid Price**" and "**Closing Sale Price**" means, for any security as of any date, the last closing bid price and last closing trade price, respectively, for such security, as reported by Bloomberg (whether or not such security is trading on an Eligible Market at such time), or, if the market on which the security is trading begins to operate on an extended hours basis and does not designate the closing bid price or the closing trade price, as the case may be, then the last bid price or last trade price, respectively, of such security prior to 4:00:00 p.m., New York Time, as reported by Bloomberg, or, if the market on which the security is trading is not the principal securities exchange or trading market for such security, the last closing bid price or last trade price, respectively, of such security on the principal securities exchange or trading market where such security is listed or traded as reported by Bloomberg, or if the foregoing do not apply, the last closing bid price or last trade price, respectively, of such security in the over-the-counter market on the electronic bulletin board for such security as reported by Bloomberg, or, if no closing bid price or last trade price, respectively, is reported for such security by Bloomberg, the average of the bid prices, or the ask prices, respectively, of any market makers for such security as reported in the "pink sheets" by Pink Sheets LLC (formerly the National Quotation Bureau, Inc.). If the Closing Bid Price or the Closing Sale Price cannot be calculated for a security on a particular date on any of the foregoing bases, the Closing Bid Price or the Closing Sale Price, as the

case may be, of such security on such date shall be the fair market value as mutually determined by the Company and the Holder. If the Company and the Holder are unable to agree upon the fair market value of such security, then such dispute shall be resolved pursuant to Section 18. All such determinations to be appropriately adjusted for any stock dividend, stock split, stock combination or other similar transaction during the applicable calculation period.

(q) "**Collateral**" has the meaning given to such term in the Security Agreement.

(r) "**Commission**" means the United States Securities and Exchange Commission.

(s) "**Common Stock**" has the meaning assigned to it in Section 3 hereof.

(t) "**Common Stock Buy-In**" has the meaning assigned to it in Section 3(c)(ii) hereof.

(u) "**Common Stock Buy-In Price**" has the meaning assigned to it in Section 3(c)(ii) hereof.

(v) "**Company Trading Day**" means any day on which the Common Stock is traded on the principal securities exchange or securities market on which the Common Stock is then traded; provided that "Company Trading Day" shall not include any day on which the Common Stock is scheduled to trade on such exchange or market for less than 4.5 hours or any day that the Common Stock is suspended from trading during the final hour of trading on such exchange or market (or if such exchange or market does not designate in advance the closing time of trading on such exchange or market, then during the hour ending at 4:00 p.m., New York Time).

(w) "**Contingent Obligation**" means, as to any Person, any direct or indirect liability, contingent or otherwise, of that Person with respect to any indebtedness, lease, dividend or other obligation of another Person if the primary purpose or intent of the Person incurring such liability, or the primary effect thereof, is to provide assurance to the obligee of such liability that such liability will be paid or discharged, or that any agreements relating thereto will be complied with, or that the holders of such liability will be protected (in whole or in part) against loss with respect thereto.

(x) "**Conversion Amount**" has the meaning assigned to it in Section 3(b) hereof.

(y) "**Conversion Date**" has the meaning assigned to it in Section 3(c)(i) hereof.

(z) "**Conversion Failure**" has the meaning assigned to it in Section 3(c)(ii) hereof.

(aa) "**Conversion Notice**" has the meaning assigned to it in Section 3(c)(i) hereof.

(bb) "**Conversion Rate**" has the meaning assigned to it in Section 3(b) hereof.

(cc) "**Convertible Securities**" means with respect to any issuer, any stock or securities (other than Options) directly or indirectly convertible into or exercisable or exchangeable for such issuer's common stock.

(dd) "**Corporate Event**" has the meaning assigned to it in Section 6(b) hereof.

(ee) "**Custodian**" has the meaning assigned to it in Section 4(a)(iv) hereof.

(ff) "**Deposit Accounts or Securities Accounts**" has the meaning assigned to it in the Security Agreement.

(gg) "**Distributed Property**" has the meaning assigned to it in Section 7(a) hereof.

(hh) "**DWAC**" has the meaning assigned to it in Section 3(c)(i) hereof.

(ii) "**Eligible Market**" means a national security exchange that has registered with the Commission under Section 6 of the Securities Exchange Act of 1934.

(jj) "**Event of Default**" has the meaning assigned to it in Section 4(a) hereof.

(kk) "**Event of Default Notice**" has the meaning assigned to it in Section 4(b) hereof.

(ll) "**Event of Default Redemption Notice**" has the meaning assigned to it in Section 4(b) hereof.

(mm) "**Event of Default Redemption Price**" has the meaning assigned to it in Section 4(b) hereof.

(nn) "**GAAP**" means U.S. generally accepted accounting principles consistently applied.

(oo) "**Holder**" has the meaning assigned to it in the introduction hereof.

(pp) "**Indebtedness**" means (1) all indebtedness for borrowed money, (2) all obligations issued, undertaken or assumed as the deferred purchase price of property or services (including, without limitation, "capital leases" in accordance with GAAP) (other

than trade payables entered into in the ordinary course of business), (3) all reimbursement or payment obligations with respect to letters of credit, surety bonds and other similar instruments, (4) all obligations evidenced by notes, bonds, debentures or similar instruments, including obligations so evidenced incurred in connection with the acquisition of property, assets or businesses, (5) all indebtedness created or arising under any conditional sale or other title retention agreement, or incurred as financing, in either case with respect to any property or assets acquired with the proceeds of such indebtedness (even though the rights and remedies of the seller or bank under such agreement in the event of default are limited to repossession or sale of such property), (6) all monetary obligations under any leasing or similar arrangement which, in connection with GAAP, consistently applied for the periods covered thereby, is classified as a capital lease, (7) all indebtedness referred to in clauses (1) through (6) above secured by (or for which the holder of such Indebtedness has an existing right, contingent or otherwise, to be secured by) any mortgage, lien, pledge, charge, security interest or other encumbrance upon or in any property or assets (including accounts and contract rights) owned by any Person, even though the Person which owns such assets or property has not assumed or become liable for the payment of such indebtedness, and (8) all Contingent Obligations in respect of indebtedness or obligations of others of the kinds referred to in clauses (1) through (7) above.

(qq) "**Initial Closing Date**" has the meaning ascribed to it in the Securities Purchase Agreement, which date is the date the Company initially issued Notes pursuant to the terms of the Securities Purchase Agreement.

(rr) "**Interest**" has the meaning assigned to it in Section 2(a) hereof.

(ss) "**Interest Date**" has the meaning assigned to it in Section 2(a) hereof.

(tt) "**Interest Election Notice**" has the meaning assigned to it in Section 2 (a) hereof.

(uu) "**Interest Notice Date**" has the meaning assigned to it in Section 2(a) hereof.

(vv) "**Interest Notice Due Date**" has the meaning assigned to it in Section 2(a) hereof.

(ww) "**Interest Rate**" means twenty percent (20.0%) per annum.

(xx) "**Issuance Date**" means April [—], 2011.

(yy) "**Liability**" means, with respect to any Person, any liability or obligation of such Person whether known or unknown, whether asserted or unasserted, whether determined, determinable or otherwise, whether absolute or contingent, whether accrued or unaccrued, whether liquidated or unliquidated, whether directly incurred or consequential, whether due or to become due and whether or not required under GAAP to be accrued on the financial statements of such Person.

(zz) "**Lien**" has the meaning assigned to it in Section 11(c) hereof.

(aaa) "**Material Adverse Effect**" has the meaning ascribed to such term in the Securities Purchase Agreement.

(bbb) "**Material Contract**" has the meaning ascribed to such term in the Securities Purchase Agreement.

(ccc) "**Maturity Date**" has the meaning assigned to it in Section 1 hereof.

(ddd) "**Maximum Percentage**" has the meaning assigned to it in Section 3(d)(i) hereof.

(eee) "**Note**" has the meaning assigned to it in the introduction hereof.

(fff) "**Note Delivery Date**" has the meaning assigned to it in Section 3(c)(i) hereof.

(ggg) "**Other Notes**" has the meaning assigned to it in the introduction hereof.

(hhh) "**Other Redemption Notice**" has the meaning assigned to it in Section 9(b) hereof.

(iii) "**Options**" means with respect to any issuer, any rights, warrants or options to subscribe for or purchase such issuer's common stock or such issuer's Convertible Securities.

(jjj) "**Parent Entity**" of a Person means an entity that, directly or indirectly, controls the applicable Person and whose common stock or equivalent equity security is quoted or listed on an Eligible Market, or, if there is more than one such Person or Parent Entity, the Person or Parent Entity with the largest public market capitalization as of the date of consummation of the Change of Control.

(kkk) "**Permitted Indebtedness**" means (1) the Indebtedness evidenced by this Note and the Other Notes (including the Additional Notes), (2) Indebtedness incurred by the Company that is made expressly subordinate in right of payment to the Indebtedness evidenced by this Note, (3) Indebtedness existing on the Effective Date and disclosed on Schedule 5.30 of the Securities Purchase Agreement, (4) Purchase Money Indebtedness, (5) Indebtedness to trade creditors incurred in the ordinary course of business, (6) extensions, refinancings and renewals of any items of Permitted Indebtedness in clauses (3) and (4) hereof, provided that the principal amount is not increased or the terms modified to impose more burdensome terms upon Company and such Indebtedness shall not be secured by any additional collateral.

(lll) "**Permitted Investments**" means (1) investments in cash, (2) investments in negotiable instruments for collection, (3) advances made in connection with purchases of goods or services in the ordinary course of business, (4) investments received in settlement of amounts due to the Company effected in the ordinary course of business or owing to the Company as a result of a proceeding of insolvency involving an account in debt to the Company or upon the foreclosure or enforcement of any Lien in favor of the Company, (5) marketable direct obligations issued or unconditionally guaranteed by the United States of America or any agency or any State thereof maturing within one (1) year from the date of acquisition thereof, (7) commercial paper maturing no more than one (1) year from the date of creation thereof and currently having rating of at least A-2 or P-2 from either Standard & Poor's Corporation or Moody's Investors Service, (8) certificates of deposit maturing no more than one year from the date of investment therein and (9) money market accounts.

(mmm) "**Permitted Liens**" means (1) any Lien for taxes not yet due or delinquent or being contested in good faith by appropriate proceedings for which adequate reserves have been established in accordance with GAAP, (2) any statutory Lien arising in the ordinary course of business by operation of law with respect to a liability that is not yet due or delinquent, (3) any Lien created by operation of law, such as materialmen's liens, mechanics' liens and other similar liens, arising in the ordinary course of business with respect to a liability that is not yet due or delinquent or that are being contested in good faith by appropriate proceedings, (4) Liens securing the Company's obligations under the Notes, (5) Liens (A) upon or in any equipment acquired or held by the Company or any of its Subsidiaries to secure the purchase price of such equipment or indebtedness incurred solely for the purpose of financing the acquisition or lease of such equipment, or (B) existing on such equipment at the time of its acquisition, provided that the Lien is confined solely to the property so acquired and improvements thereon, and the proceeds of such equipment, (6) Liens incurred in connection with the extension, renewal or refinancing of the indebtedness secured by Liens of the type described in clauses (1) through (5) above, provided that any extension, renewal or replacement Lien shall be limited to the property encumbered by the existing Lien and the principal amount of the Indebtedness being extended, renewed or refinanced does not increase, (7) leases, subleases, licenses and sublicenses granted to others in the ordinary course of the Company's business, not interfering in any material respect with the business of the Company and its Subsidiaries taken as a whole, (8) Liens in favor of customs and revenue authorities arising as a matter of law to secure payments of custom duties in connection with the importation of goods, (9) Liens arising from judgments, decrees or attachments in circumstances not constituting an Event of Default under Section 4(a)(vi) and (10) Liens of King George Holdings Luxembourg IIA S.à.r.l. or any affiliate thereof existing as of the Effective Date.

(nnn) "**Person**" means and includes all natural persons, corporations, business trusts, associations, companies, partnerships, joint ventures, limited liability companies and other entities and governments and agencies and political subdivisions.

(ooo) "**PIK Interest**" has the meaning assigned to it in Section 2(a) hereof.

(ppp) "**Principal**" has the meaning assigned to it in the introduction hereof.

(qqq) "**Purchase Money Indebtedness**" means Indebtedness (other than the Secured Obligations, but including capital lease obligations as defined under GAAP), incurred at the time of, or within 20 days after, the acquisition of any fixed assets for the purpose of financing all or any part of the acquisition cost thereof; provided, such Indebtedness shall not exceed $50,000 in the aggregate.

(rrr) "**Purchase Rights**" has the meaning assigned to it in Section 6(a) hereof.

(sss) "**Redemption Multiplier**" shall equal two (2).

(ttt) "**Redemption Price**" means either an Event of Default Redemption Price or Change of Control Redemption Price.

(uuu) "**Register**" has the meaning assigned to it in Section 25 hereof.

(vvv) "**Required Holders**" means the holders of Notes representing at least a majority of the aggregate principal amount of the Notes then outstanding.

(www) "**Secured Obligations**" has the meaning assigned to it in the Security Agreement.

(xxx) "**Security Agreement**" means that certain security agreement dated as of the Securities Purchase Agreement initially by and among A.P. Pharma, Inc., Tang Capital Partners, LP, Baker Bros. Investments II, L.P., Baker Brothers Life Sciences, L.P. and 14159, L.P., pursuant to which the Notes were secured.

(yyy) "**Securities Purchase Agreement**" means that certain securities purchase agreement dated as of the Subscription Date by and among A.P. Pharma, Inc., Tang Capital Partners, LP, Baker Bros. Investments II, L.P., Baker Brothers Life Sciences, L.P. and 14159, L.P., pursuant to which the Company issued the Notes.

(zzz) "**Share Delivery Date**" has the meaning assigned to it in Section 3(c)(i) hereof.

(aaaa) "**Subscription Date**" means April 24, 2011.

(bbbb) "**Successor Entity**" means the Person, which may be the Company, formed by, resulting from or surviving any Change of Control or the Person with which such Change of Control shall have been made, provided that if such Person is not a publicly traded entity whose common stock or equivalent equity security is quoted or listed for trading on an Eligible Market, Successor Entity shall mean such Person's Parent Entity.

(cccc) "**Trading Day**" means any day on which the Common Stock is traded on the Principal Market, or, if the Principal Market is not the principal trading market for the Common Stock, then on the principal securities exchange or securities market on which the Common Stock is then traded; provided that "Trading Day" shall not include any day on which the Common Stock is scheduled to trade on such exchange or market for less than 4.5 hours or any day that the Common Stock is suspended from trading during the final hour of trading on such exchange or market (or if such exchange or market does not designate in advance the closing time of trading on such exchange or market, then during the hour ending at 4:00:00 p.m., New York Time).

(dddd) "**Transaction Documents**" has the meaning ascribed to such term in the Securities Purchase Agreement.

(24) SECURITY. The Notes shall be secured by and to the extent provided in the Security Agreement.

(25) REGISTERED OBLIGATION. The Company shall establish and maintain a record of ownership (the "**Register**") in which it will register by book entry the interest of the initial Holder and of each subsequent assignee in this Note, and in the right to receive any payments of principal and interest or any other payments hereunder, and any assignment of any such interest. Notwithstanding anything herein to the contrary, this Note is intended to be treated as a registered obligation for federal income tax purposes and the right, title, and interest of the Holder and its assignees in and to payments under this Note shall be transferable only upon notation of such transfer in the Register. This Section shall be construed so that the Note is at all times maintained in "registered form" within the meaning of Sections 163(f), 871(h)(2) and 881(c)(2) of the Internal Revenue Code and any related regulations (or any successor provisions of the Code or such regulations).

[Signature Page Follows]

IN WITNESS WHEREOF, the Company has caused this Note to be duly executed as of the Issuance Date set out above.

A.P. PHARMA, INC.

By: _____
Name: John Whelan
Title: Chief Executive Officer

EXHIBIT I

A.P. PHARMA, INC.
CONVERSION NOTICE

TO BE EXECUTED BY THE REGISTERED HOLDER TO CONVERT THIS NOTE INTO COMMON STOCK

Reference is made to the Senior Secured Convertible Note due 2021 (the "**Note**") issued to the undersigned by A.P. Pharma, Inc. (the "**Company**"). In accordance with and pursuant to the Note, the undersigned hereby elects to convert the Conversion Amount (as defined in the Note) of the Note indicated below into shares of Common Stock, par value $0.01 per share (the "**Common Stock**"), of the Company as of the date specified below. The undersigned hereby makes the representations and warranties set forth in Section 4 of the Securities Purchase Agreement.

Date of Conversion: _____

Aggregate Conversion Amount to be converted: _____

Please confirm the following information:

Conversion Rate: _____

Number of shares of Common Stock to be issued: _____

Common Stock Beneficially Owned: _____

Please issue the Common Stock into which the Note is being converted in the following name and to the following address:

Issue to: _____

_____

_____

Facsimile Number: _____

Authorization: _____

By: _____

Title: _____

Dated: _____

Account Number: _____
(if electronic book entry transfer)

Transaction Code Number: _____
(if electronic book entry transfer)

ACKNOWLEDGMENT

The Company hereby acknowledges this Conversion Notice and hereby directs _____, the Company's transfer agent (the "**Transfer Agent**"), to issue the above indicated number of shares of Common Stock in accordance with the Transfer Agent Instructions dated _____ __, 20__ from the Company and acknowledged and agreed to by Transfer Agent.

A.P. PHARMA, INC.

By: _____
Name:
Title:

Exhibit 10.3

SECURITY AGREEMENT

This **SECURITY AGREEMENT** (this "Agreement"), dated as of April 24, 2011 among **A.P. PHARMA, INC.** and those additional entities that hereafter become parties hereto by executing the form of Supplement attached hereto as Annex 1 ("Grantor"), and **TANG CAPITAL PARTNERS, LP,** in its capacity as representative of the Purchasers (together with its successors, "Agent").

RECITALS

WHEREAS, Pursuant to that certain Securities Purchase Agreement, dated as of April 24, 2011 (the "Securities Purchase Agreement"), by and among A.P. Pharma, Inc. ("Debtor"), Tang Capital Partners, LP and Baker Bros. Investments II, L.P., Baker Brothers Life Sciences, L.P., and 14159, L.P., each as a Purchaser (collectively, the "Purchasers" and individually, a "Purchaser"), Debtor has agreed to issue to the Purchasers, and the Purchasers have agreed to purchase from Debtor, the Notes, and

WHEREAS, This Security Agreement is integral to the transactions contemplated by the Securities Purchase Agreement and the Notes, and the execution and delivery hereof are conditions precedent to the willingness of Purchasers to purchase and extend credit under the Notes,

WHEREAS, Agent has agreed to act as agent for the benefit of the Purchaser Group in connection with this Agreement; and

NOW, THEREFORE, for and in consideration of the recitals made above and other good and valuable consideration, the receipt, sufficiency and adequacy of which are hereby acknowledged, the parties hereto agree as follows:

1. Defined Terms. All capitalized terms used herein (including in the preamble and recitals hereof) without definition shall have the meanings ascribed thereto in the Securities Purchase Agreement and the Notes, as the context requires. Any terms used in this Agreement that are defined in the Code shall be construed and defined as set forth in the Code unless otherwise defined herein or in the Securities Purchase Agreement or the Notes; provided, however, that if the Code is used to define any term used herein and if such term is defined differently in different Articles of the Code, the definition of such term contained in Article 9 of the Code shall govern. In addition to those terms defined elsewhere in this Agreement, as used in this Agreement, the following terms shall have the following meanings:

(a) "Account" means an account (as that term is defined in the Code).

(b) "Account Debtor" means an account debtor (as that term is defined in the Code).

(c) "Agent" has the meaning specified in the preamble hereto.

(d) "Agent's Liens" means the Liens granted by Grantor to the Purchasers and Agent pursuant to this Agreement.

(e) "Bankruptcy Law" has the meaning specified in the Securities Purchase Agreement.

(f) "Books" means books and records (including Grantor's Records indicating, summarizing, or evidencing Grantor's assets (including the Collateral) or liabilities, Grantor's Records relating to Grantor's business operations or financial condition, and Grantor's goods or General Intangibles related to such information).

(g) "Chattel Paper" means chattel paper (as that term is defined in the Code) and includes tangible chattel paper and electronic chattel paper.

(h) "Code" means the Delaware Uniform Commercial Code, as in effect from time to time; provided, however, that in the event that, by reason of mandatory provisions of law, any or all of the attachment, perfection, priority, or remedies with respect to Agent's Lien on any Collateral is governed by the Uniform Commercial Code as enacted and in effect in a jurisdiction other than the State of Delaware, the term "Code" shall mean the Uniform Commercial Code as enacted and in effect in such other jurisdiction solely for purposes of the provisions thereof relating to such attachment, perfection, priority, or remedies.

(i) "Collateral" has the meaning specified in Section 2.

(j) "Commercial Tort Claims" means commercial tort claims (as that term is defined in the Code), and includes those commercial tort claims listed on Schedule 1 attached hereto ("Commercial Tort Claims").

(k) "Control Agreement" means a deposit account control agreement or securities account control agreement that provides Agent with "control" in accordance with Sections 8-106, 9-104, 9-105, 9-106, and 9-107 of the Code and otherwise in such form reasonably acceptable to Agent.

(l) "Copyrights" means copyrights and copyright registrations, and also includes (i) any copyright registrations and recordings thereof and all applications in connection therewith, (ii) all reissues, continuations, extensions or renewals thereof, (iii) all income, royalties, damages and payments now and hereafter due or payable under and with respect thereto, including payments under all licenses entered into in connection therewith and damages and payments for past or future infringements or dilutions thereof, (iv) the right to sue for past, present and future infringements and dilutions thereof, (v) the goodwill of Grantor's business symbolized by the foregoing or connected therewith, and (vi) all of Grantor's rights corresponding thereto throughout the world.

(m) "Deposit Account" means a deposit account (as that term is defined in the Code) other than the Excluded Deposit Account.

(n) "Environmental Laws" has the meaning specified in the Securities Purchase Agreement.

(o) "Equipment" means equipment (as that term is defined in the Code).

(p) "Event of Default" has the meaning specified in the Notes.

(q) "Excluded Deposit Account" means the Wells Fargo checking account number 028-5064622, provided that to the extent the amount deposited in such account exceeds $314,715, then such account shall become a "Deposit Account" for all purposes hereunder.

(r) "Expenses" means all (a) out-of pocket costs or expenses (including taxes, and insurance premiums) required to be paid by Debtor under any of the Note Documents that are paid, advanced, or incurred by the Purchaser Group in accordance with the terms of this Agreement and the other Note Documents, (b) out-of-pocket fees or charges paid or incurred by Agent in connection with the Purchaser Group's transactions with Debtor, including, fees or charges for photocopying, notarization, couriers and messengers, telecommunication, public record searches (including tax lien, litigation, and UCC searches and including searches with the patent and trademark office, the copyright office, or the department of motor vehicles), filing, recording, publication, appraisal (including periodic collateral appraisals or business valuations to the extent of the fees and charges (and up to the amount of any limitation) contained in the Agreement), (c) out-of pocket costs and expenses incurred by Agent in the disbursement of funds to Debtor or other members of the Purchaser Group (by wire transfer or otherwise), (d) out-of pocket charges paid or incurred by Agent resulting from the dishonor of checks, (e) reasonable costs and expenses paid or incurred by the Purchaser Group to correct any default or enforce any provision of the Note Documents, or in gaining possession of, maintaining, handling, preserving, storing, shipping, selling, preparing for sale, or advertising to sell the Collateral, or any portion thereof, irrespective of whether a sale is consummated, (f) out-of pocket audit fees and expenses (including travel, meals, and lodging) of Agent related to any inspections or audits to the extent of the fees and charges (and up to the amount of any limitation) contained in the Note Documents, (g) reasonable costs and expenses of third party claims or any other suit paid or incurred by the Purchaser Group in enforcing or defending the Note Documents or in connection with the transactions contemplated by the Note Documents or the Purchaser Group's relationship Debtor, (h) Agent's and each Purchaser's reasonable costs and expenses (including attorneys fees) incurred in advising, structuring, drafting, reviewing, administering (including travel, meals, and lodging) or amending the Note Documents, and (i) Agent's and each Purchaser's reasonable costs and expenses (including attorneys, accountants, consultants, and other advisors fees and expenses) incurred in terminating, enforcing (including attorneys, accountants, consultants, and other advisors fees and expenses incurred in connection with a "workout," a "restructuring," or an Insolvency Proceeding concerning Debtor or in exercising rights or remedies under the Note Documents), or defending the Note Documents, irrespective of whether suit is brought, or in taking any Remedial Action concerning the Collateral; provided that, notwithstanding anything herein to the contrary, the fees and

expenses specified in this definition do not include fees and expenses solely related to the Agent's or any Purchasers' role as an equity investor of Debtor.

(s) "General Intangibles" means general intangibles (as that term is defined in the Code) and, in any event, includes payment intangibles, contract rights, rights to payment, rights arising under common law, statutes, or regulations, choses or things in action, goodwill (including the goodwill associated with any Trademark, Patent, or Copyright), Patents, Trademarks, Copyrights, URLs and domain names, industrial designs, other industrial or Intellectual Property or rights therein or applications therefor, whether under license or otherwise, programs, programming materials, blueprints, drawings, purchase orders, customer lists, monies due or recoverable from pension funds, route lists, rights to payment and other rights under any royalty or licensing agreements, including Intellectual Property Licenses, infringement claims, computer programs, information contained on computer disks or tapes, software, literature, reports, catalogs, pension plan refunds, pension plan refund claims, insurance premium rebates, tax refunds, and tax refund claims, interests in a partnership or limited liability company which do not constitute a security under Article 8 of the Code, and any other personal property other than Commercial Tort Claims, money, Accounts, Chattel Paper, Deposit Accounts, goods, Investment Related Property, Negotiable Collateral, and oil, gas, or other minerals before extraction.

(t) "Goods" means goods (as that term is defined in the Code).

(u) "Grantor" has the meaning specified in the recitals to this Agreement.

(v) "Hazardous Materials" has the meaning specified in the Securities Purchase Agreement.

(w) "Insolvency Proceeding" means any proceeding commenced by or against any Person under any provision of the Bankruptcy Law or under any other state or federal bankruptcy or insolvency law, assignments for the benefit of creditors, formal or informal moratoria, compositions, extensions generally with creditors, or proceedings seeking reorganization, arrangement, or other similar relief.

(x) "Intellectual Property" means the Patents, Copyrights, Trademarks, the goodwill associated with such Trademarks, trade secrets and customer lists, and Intellectual Property Licenses, in each case other than the King George Property, but solely during such time that the King George Property is subject to the lien described in the definition thereof.

(y) "Intellectual Property Licenses" means rights under or interests in any patent, trademark, copyright or other intellectual property, including software license agreements with any other party, whether Grantor is a licensee or licensor under any such license agreement, including the license agreements listed on Schedule 2 attached hereto and made a part hereof, in each case other than the King George Property, but solely during such time that the King George Property is subject to the lien described in the definition thereof.

(z) "Inventory" means inventory (as that term is defined in the Code).

(aa) "Investment Related Property" means (i) investment property (as that term is defined in the Code), and (ii) all of the following (regardless of whether classified as investment property under the Code): all Pledged Interests, Pledged Operating Agreements, and Pledged Partnership Agreements.

(bb) "King George Property" means the collateral in which King George Holdings Luxembourg IIA S.à r.l. ("King George") has received a security interest pursuant to that certain Security Agreement dated as of January 17, 2006 by and between Debtor and King George.

(cc) "Mortgages" means, individually and collectively, one or more mortgages, deeds of trust, or deeds to secure debt, executed and delivered by Grantor in favor of Agent, in form and substance satisfactory to Agent, that encumber the Real Property.

(dd) "Note Document" means the Securities Purchase Agreement, Notes, this Agreement, the Patent Security Agreement and any other agreement entered into, now or in the future, by Debtor and in connection with the Securities Purchase Agreement or Notes.

(ee) "Notes" shall have the meaning set forth in the Securities Purchase Agreement.

(ff) "Negotiable Collateral" means letters of credit, letter-of-credit rights, instruments, promissory notes, drafts, and documents.

(gg) "Patents" means patents and patent applications, and also includes (i) the patents and patent applications listed on Schedule 3 attached hereto and made a part hereof, (ii) all renewals thereof, (iii) all income, royalties, damages and payments now and hereafter due or payable under and with respect thereto, including payments under all licenses entered into in connection therewith and damages and payments for past or future infringements or dilutions thereof, (iv) the right to sue for past, present and future infringements and dilutions thereof, and (v) all of Grantor's rights corresponding thereto throughout the world, in each case other than the King George Property, but solely during such time that the King George Property is subject to the lien described in the definition thereof.

(hh) "Patent Security Agreement" means each Patent Security Agreement among Grantor and Agent, in substantially the form of Exhibit A attached hereto, pursuant to which Grantor has granted to the Purchaser Group a security interest in all its Patents.

(ii) "Permitted Liens" shall have the meaning set forth in the Notes.

(jj) "Person" has the meaning specified in the Securities Purchase Agreement.

(kk) "Pledged Companies" means, each Person listed on Schedule 4 hereto as a "Pledged Company", together with each other Person, all or a portion of whose Stock, is acquired or otherwise owned by Grantor after the date hereof.

(ll) "Pledged Interests" means all of Grantor's right, title and interest in and to all of the Stock now or hereafter owned by Grantor, regardless of class or designation, including all substitutions therefor and replacements thereof, all proceeds thereof and all rights relating thereto, also including any certificates representing the Stock, the right to receive any certificates representing any of the Stock, all warrants, options, share appreciation rights and other rights, contractual or otherwise, in respect thereof, and the right to receive dividends, distributions of income, profits, surplus, or other compensation by way of income or liquidating distributions, in cash or in kind, and cash, instruments, and other property from time to time received, receivable, or otherwise distributed in respect of or in addition to, in substitution of, on account of, or in exchange for any or all of the foregoing.

(mm) "Pledged Interests Addendum" means a Pledged Interests Addendum substantially in the form of Exhibit B to this Agreement.

(nn) "Pledged Operating Agreements" means all of Grantor's rights, powers, and remedies under the limited liability company operating agreements of each of the Pledged Companies that are limited liability companies.

(oo) "Pledged Partnership Agreements" means all of Grantor's rights, powers, and remedies under the partnership agreements of each of the Pledged Companies that are partnerships.

(pp) "Proceeds" has the meaning specified in Section 2.

(qq) "Purchaser" has the meaning specified in the preamble hereto.

(rr) "Purchaser Group" means, individually and collectively, each of the Purchasers and Agent.

(ss) "Real Property" means any estates or interests in real property now owned or hereafter acquired by Grantor and the improvements thereto.

(tt) "Records" means information that is inscribed on a tangible medium or which is stored in an electronic or other medium and is retrievable in perceivable form.

(uu) "Remedial Action" means all actions taken to (a) clean up, remove, remediate, contain, treat, monitor, assess, evaluate, or in any way address Hazardous Materials in the indoor or outdoor environment, (b) prevent or minimize a release or threatened release of Hazardous Materials so they do not migrate or endanger or threaten to endanger public health or welfare or the indoor or outdoor environment, (c) restore or reclaim natural resources or the environment, (d) perform any pre-remedial studies,

investigations, or post-remedial operation and maintenance activities, or (e) conduct any other actions with respect to Hazardous Materials authorized by Environmental Laws.

(vv) "Security Interest" has the meaning specified in Section 2.

(ww) "Secured Obligations" means each and all of the following: all of the present and future indebtedness, liabilities, and obligations of Grantor arising from this Agreement, the Notes, or the other Note Documents, including attorneys fees and expenses and any interest, fees, or expenses that accrue after the filing of an Insolvency Proceeding, regardless of whether allowed or allowable in whole or in part as a claim in any Insolvency Proceeding. The Secured Obligation shall include, without limitation, future, as well as existing indebtedness, liabilities, and obligations owed by Debtor to the holders of the Notes arising under the Notes and this Security Agreement, provided that, for the avoidance doubt, "Secured Obligations" shall not include any obligations solely related to any Stock (including Stock upon conversion of the Notes pursuant to the terms thereof) held by the Purchasers in their capacity solely as shareholders.

(xx) "Securities Account" means a securities account (as that term is defined in the Code).

(yy) "Securities Purchase Agreement" has the meaning specified in the recitals to this Agreement.

(zz) "Stock" means all shares, options, warrants, interests, participations, or other equivalents (regardless of how designated) of or in a Person, whether voting or nonvoting, including common stock, preferred stock, or any other "equity security" (as such term is defined in Rule 3a11-1 of the General Rules and Regulations promulgated by the SEC under the Exchange Act).

(aaa) "Supporting Obligations" means supporting obligations (as such term is defined in the Code).

(bbb) "Trademarks" means trademarks, trade names, trademark applications, service marks, service mark applications, and also includes (i) all renewals thereof, (ii) all income, royalties, damages and payments now and hereafter due or payable under and with respect thereto, including payments under all licenses entered into in connection therewith and damages and payments for past or future infringements or dilutions thereof, (iii) the right to sue for past, present and future infringements and dilutions thereof, (iv) the goodwill of Grantor's business symbolized by the foregoing or connected therewith, and (v) all of Grantor's rights corresponding thereto throughout the world.

(ccc) "URL" means "uniform resource locator," an internet web address.

2. Grant of Security. Grantor hereby unconditionally grants, assigns, and pledges to Agent, for the benefit of the Purchasers, a continuing security interest (herein referred to as the "Security Interest") in all personal property of Grantor whether now owned

or hereafter acquired or arising and wherever located, including Grantor's right, title, and interest in and to the following, whether now owned or hereafter acquired or arising and wherever located (the "Collateral"):

(a) all of Grantor's Accounts;

(b) all of Grantor's Books;

(c) all of Grantor's Chattel Paper;

(d) all of Grantor's Deposit Accounts;

(e) all of Grantor's Equipment and fixtures;

(f) all of Grantor's General Intangibles;

(g) all of Grantor's Goods;

(h) all of Grantor's Inventory;

(i) all of Grantor's Investment Related Property;

(j) all of Grantor's Negotiable Collateral;

(k) all of Grantor's rights in respect of Supporting Obligations;

(l) all of Grantor's Commercial Tort Claims;

(m) all of Grantor's money or other assets of Grantor that now or hereafter come into the possession, custody, or control of Agent or any Purchaser;

(n) all of the proceeds and products, whether tangible or intangible, of any of the foregoing, including proceeds of insurance or Commercial Tort Claims covering or relating to any or all of the foregoing, and any and all Accounts, Books, Chattel Paper, Deposit Accounts, Equipment, General Intangibles, Inventory, Investment Related Property, Negotiable Collateral, Supporting Obligations, money, or other tangible or intangible property resulting from the sale, lease, license, exchange, collection, or other disposition of any of the foregoing, the proceeds of any award in condemnation with respect to any of the foregoing, any rebates or refunds, whether for taxes or otherwise, and all proceeds of any such proceeds, or any portion thereof or interest therein, and the proceeds thereof, and all proceeds of any loss of, damage to, or destruction of the above, whether insured or not insured, and, to the extent not otherwise included, any indemnity, warranty, or guaranty payable by reason of loss or damage to, or otherwise with respect to any of the foregoing (the "Proceeds"). Without limiting the generality of the foregoing, the term "Proceeds" includes whatever is receivable or received when Investment Related Property or proceeds are sold, exchanged, collected, or otherwise disposed of, whether such disposition is voluntary or

involuntary, and includes proceeds of any indemnity or guaranty payable to Grantor or Agent from time to time with respect to any of the Investment Related Property.

Notwithstanding anything contained in this Agreement to the contrary, the term "Collateral" shall not include (i) any rights or interest in any contract, lease, permit, license, charter or license agreement covering personal property of Grantor if under the terms of such contract, lease, permit, license, charter or license agreement, or applicable law with respect thereto, the grant of a security interest or lien therein is prohibited as a matter of law or under the terms of such contract, lease, permit, license, charter or license agreement and such prohibition has not been waived or the consent of the other party to such contract, lease, permit, license, charter or license agreement has not been obtained (provided, that, the foregoing exclusions shall in no way be construed (A) to apply to the extent that any described prohibition is unenforceable under Section 9-406, 9-407, 9-408, or 9-409 of the Code or other applicable law, (B) to limit, impair, or otherwise affect the Purchaser Group's continuing security interests in and liens upon any rights or interests of Grantor in or to (x) monies due or to become due under any described contract, lease, permit, license, charter or license agreement (including any Accounts), or (y) any proceeds from the sale, license, lease, or other dispositions of any such contract, lease, permit, license, charter, license agreement, or Stock, or (C) apply to the extent that any consent or waiver has been obtained that would permit the security interest of lien notwithstanding the prohibition), (ii) more than sixty five percent (65%) of the Stock of a foreign Subsidiary of Grantor, if and to the extent a grant of a security interest in such Stock would result in repatriation of earnings to Grantor pursuant to Section 956 of the Internal Revenue Code; and (iii) the King George Property but solely during such time that the King George Property is subject to the lien described in the definition thereof.

3. Security for Obligations. This Agreement and the Security Interest created hereby secures the payment and performance of the Secured Obligations, whether now existing or arising hereafter. Without limiting the generality of the foregoing, this Agreement secures the payment of all amounts which constitute part of the Secured Obligations and would be owed by Grantor to Agent or the Purchasers, but for the fact that they are unenforceable or not allowable due to the existence of an Insolvency Proceeding involving Grantor.

4. Grantor Remain Liable. Anything herein to the contrary notwithstanding, (a) Grantor shall remain liable under the contracts and agreements included in the Collateral, including the Pledged Operating Agreements and the Pledged Partnership Agreements, to perform all of the duties and obligations thereunder to the same extent as if this Agreement had not been executed, (b) the exercise by Agent or any member of the Purchaser Group of any of the rights hereunder shall not release Grantor from any of its duties or obligations under such contracts and agreements included in the Collateral, and (c) none of the members of the Purchaser Group shall have any obligation or liability under such contracts and agreements included in the Collateral by reason of this Agreement, nor shall any member of the Purchaser Group be obligated to perform any of the obligations or duties of Grantor thereunder or to take any action to collect or enforce any claim for payment

assigned hereunder. Until an Event of Default shall occur and be continuing, except as otherwise provided in this Agreement, the Securities Purchase Agreement, or other Note Documents, Grantor shall have the right to possession and enjoyment of the Collateral for the purpose of conducting the ordinary course of its businesses, subject to and upon the terms hereof and of the Notes, the Securities Purchase Agreement and the other Note Documents. Without limiting the generality of the foregoing, it is the intention of the parties hereto that record and beneficial ownership of the Pledged Interests, including all voting, consensual, and dividend rights, shall remain in Grantor until the occurrence of an Event of Default and until Agent shall notify Grantor of Agent's exercise of voting, consensual, or dividend rights with respect to the Pledged Interests pursuant to Section 16 hereof.

5. Representations and Warranties. Grantor hereby represents and warrants as follows:

(a) The exact legal name of Grantor is set forth on the signature pages of this Agreement.

(b) Grantor does not own any Real Property as of the date hereof and Grantor has no copyrights that have been registered with the United States Copyright Office.

(c) As of the date hereof, Grantor has no interest in, or title to, any Intellectual Property Licenses or Patents, except as set forth on Schedules 2 and 3, respectively, attached hereto. This Agreement is effective to create a valid and continuing Lien on such Intellectual Property Licenses and Patents and, upon filing of the Patent Security Agreement with the United State Patent and Trademark Office, and the filing of appropriate financing statements in the jurisdictions listed on Schedule 5 hereto, all action necessary to perfect the Security Interest in and to on Grantor's Patents has been taken and such perfected Security Interest is enforceable as such as against any and all creditors of and purchasers from Grantor.

(d) This Agreement creates a valid security interest in the Collateral of Grantor, to the extent a security interest therein can be created under the Code, securing the payment of the Secured Obligations. Except to the extent a security interest in the Collateral cannot be perfected by the filing of a financing statement under the Code, all filings and other actions necessary (other than entry into Control Agreements on the Initial Closing Date) to perfect such security interest have been duly taken or will have been taken upon the filing of financing statements listing Grantor, as a debtor, and Agent, as secured party, in the jurisdictions listed next to Grantor's name on Schedule 5 attached hereto. Upon the making of such filings, Agent shall have a first priority (subject to Permitted Liens) perfected security interest in the Collateral of Grantor to the extent such security interest can be perfected by the filing of a financing statement. As of the Initial Closing Date and each Subsequent Closing Date, all action by Grantor reasonably necessary to perfect such security interest on each item of Collateral has been duly taken.

(e) (i) Except for the Security Interest created hereby, Grantor is and will at all times be the sole holder of record and the legal and beneficial owner, free and clear of all Liens other than Permitted Liens, of the Pledged Interests indicated on Schedule 4 as being owned by Grantor and, when acquired by Grantor, any Pledged Interests acquired after the date hereof; (ii) all of the Pledged Interests are duly authorized, validly issued, fully paid and nonassessable and the Pledged Interests constitute or will constitute the percentage of the issued and outstanding Stock of the Pledged Companies of Grantor identified on Schedule 4 hereto as supplemented or modified by any Pledged Interests Addendum or any Supplement to this Agreement; (iii) Grantor has the right and requisite authority to pledge the Investment Related Property pledged by Grantor to Agent as provided herein; (iv) all actions necessary to perfect, establish the first priority (subject to Permitted Liens) of, Agent's Liens in the Investment Related Collateral, and the proceeds thereof, have been duly taken, (A) upon the execution and delivery of this Agreement; (B) upon the taking of possession by Agent of any certificates constituting the Pledged Interests, to the extent such Pledged Interests are represented by certificates, together with undated powers endorsed in blank by Grantor; (C) upon the filing of financing statements in the applicable jurisdiction set forth on Schedule 5 attached hereto for Grantor with respect to the Pledged Interests of Grantor that are not represented by certificates, and (D) with respect to any Securities Accounts, upon the delivery of Control Agreements with respect thereto; and (v) Grantor has delivered to and deposited with Agent (or, with respect to any Pledged Interests created or obtained after the date hereof, will deliver and deposit in accordance with Sections 6(a) and 8 hereof) all certificates representing the Pledged Interests owned by Grantor to the extent such Pledged Interests are represented by certificates, and undated powers endorsed in blank with respect to such certificates. None of the Pledged Interests owned or held by Grantor has been issued or transferred in violation of any securities registration, securities disclosure, or similar laws of any jurisdiction to which such issuance or transfer may be subject.

(f) The Security Interest created hereby upon completion of the filings and other actions specified Schedule 6 attached hereto (which, in the case of all filings and other documents referred to on Schedule 6, have been delivered to Agent in completed an duly executed form) will constitute valid perfected security interests in all the Collateral in favor of Agent, enforceable as such as against any and all creditors of and purchasers from Grantor in accordance with the terms hereof and (b) are prior to all other Liens on the Collateral in existence on the date hereof except for Permitted Liens. The fillings and other actions specified on Schedule 6 constitute all of the filings and other actions necessary to perfect all Security Interests granted hereunder.

(g) No consent, approval, authorization, or other order or other action by, and no notice to or filing with, any Governmental Authority or any other Person is required (i) for the grant of a Security Interest by Grantor in and to the Collateral pursuant to this Agreement or for the execution, delivery, or performance of this Agreement by Grantor, or (ii) for the exercise by Agent of the voting or other rights provided for in this Agreement with respect to the Investment Related Property or the remedies in respect of the Collateral pursuant to this Agreement, except as may be required in connection with such disposition of Investment Related Property by laws affecting the offering and sale of securities generally.

(h) Grantor does not own any motor vehicles.

(i) All Deposit Accounts and all other depositary and other accounts maintained by Grantor as of the date hereof are described on Schedule 7 attached hereto.

6. Covenants. Grantor, jointly and severally, covenants and agrees with Agent that from and after the date of this Agreement and until the date of termination of this Agreement in accordance with Section 23 hereof:

(a) Possession of Collateral. In the event that any Collateral, including proceeds, is evidenced by or consists of Negotiable Collateral, Investment Related Property, or Chattel Paper, in each case with a value in excess of $5,000 individually and $25,000 in the aggregate, and if and to the extent that perfection or priority of Agent's Security Interest is dependent on or enhanced by possession, Grantor, immediately upon the request of Agent, shall execute such other documents and instruments as shall be requested by Agent or, if applicable, endorse and deliver physical possession of such Negotiable Collateral, Investment Related Property, or Chattel Paper to Agent, together with such undated powers endorsed in blank as shall be requested by Agent;

(b) Chattel Paper.

(i) Control Agreements. Grantor shall take all steps reasonably necessary to grant Agent control of all electronic Chattel Paper in accordance with the Code and all "transferable records" as that term is defined in Section 16 of the Uniform Electronic Transaction Act and Section 201 of the federal Electronic Signatures in Global and National Commerce Act as in effect in any relevant jurisdiction;

(ii) If Grantor retains possession of any Chattel Paper or instruments (which retention of possession shall be subject to the extent permitted hereby), promptly upon the request of Agent, such Chattel Paper and instruments shall be marked with the following legend: "This writing and the obligations evidenced or secured hereby are subject to the Security Interest of Tang Capital Partners, LP, as Agent for the Purchasers";

(c) Control Agreements; Deposit Accounts.

(i) On or before the Initial Closing Date, Grantor shall obtain an authenticated Control Agreement, from each bank maintaining a Deposit Account for Grantor;

(ii) On or before the Initial Closing Date, Grantor shall obtain authenticated Control Agreements, from each issuer of uncertificated securities, securities intermediary, or commodities intermediary issuing or holding any financial assets or commodities to or for Grantor

(iii) Grantor shall close the Excluded Account immediately upon confirmation that all checks outstanding as of April 25, 2011 have cleared;

(d) Letter-of-Credit Rights. Grantor that is or becomes the beneficiary of a letter of credit with a face value in excess of $25,000 in the aggregate (excluding a letter of credit that is a Supporting Obligation) shall promptly (and in any event within 5 Business Days after becoming a beneficiary), notify Agent thereof and, upon the request by Agent, enter into a tri-party agreement with Agent and the issuer or confirmation bank with respect to letter-of-credit rights assigning such letter-of-credit rights to Agent and directing, during the continuance of an Event of Default all payments thereunder to Agent's Account, all in form and substance satisfactory to Agent;

(e) Commercial Tort Claims. Grantor shall promptly (and in any event within 5 Business Days of receipt thereof), notify Agent in writing upon incurring or otherwise obtaining a Commercial Tort Claim which is reasonably expected to have value in excess of $25,000 after the date hereof and, upon request of Agent, promptly amend Schedule 1 to this Agreement to describe such after-acquired Commercial Tort Claim in a manner that reasonably identifies such Commercial Tort Claim, and hereby authorizes the filing of additional financing statements or amendments to existing financing statements describing such Commercial Tort Claims, and agrees to do such other acts or things deemed necessary or desirable by Agent to give Agent a first priority (subject to Permitted Liens), perfected security interest in any such Commercial Tort Claim;

(f) Government Contracts. If any Account or Chattel Paper arises out of a contract or contracts with the United States of America or any department, agency, or instrumentality thereof with a value in excess of $25,000 in the aggregate, Grantor shall promptly (and in any event within 5 Business Days of the creation thereof) notify Agent thereof in writing and execute any instruments or take any steps reasonably required by Agent in order that all moneys due or to become due under such contract or contracts shall be assigned to Agent, for the benefit of the Purchaser Group and shall provide written notice thereof under the Assignment of Claims Act or other applicable law;

(g) Intellectual Property.

(i) Upon the request of Agent, in order to facilitate filings with the United States Patent and Trademark Office, Grantor shall execute and deliver to Agent one or more Patent Security Agreements to further evidence Agent's Lien on Grantor's Patents and the General Intangibles of Grantor relating thereto or represented thereby;

(ii) Grantor shall have the duty, to the extent necessary or economically desirable in the operation of Grantor's business, (A) to promptly sue for infringement, misappropriation, or dilution and to recover any and all damages for such infringement, misappropriation, or dilution, (B) to prosecute diligently any trademark application or service mark application that is part of the Trademarks

pending as of the date hereof or hereafter until the termination of this Agreement, (C) to prosecute diligently any patent application that is part of the Patents pending as of the date hereof or hereafter until the termination of this Agreement, and (D) to take all reasonable and necessary action to preserve and maintain all of Grantor's Trademarks, Patents, Copyrights, Intellectual Property Licenses, and its rights therein, including the filing of applications for renewal, affidavits of use, affidavits of noncontestability and opposition and interference and cancellation proceedings. Grantor further agrees not to abandon any Trademark, Patent, Copyright, or Intellectual Property License that is necessary in the operation of Grantor's business;

(iii) Grantor acknowledges and agrees that Agent shall have no duties with respect to the Trademarks, Patents, Copyrights, or Intellectual Property Licenses. Without limiting the generality of this Section 6(g), Grantor acknowledges and agrees that no member of the Purchaser Group shall be under any obligation to take any steps necessary to preserve rights in the Trademarks, Patents, Copyrights, or Intellectual Property Licenses against any other Person, but Agent may do so at its option from and after the occurrence and during the continuance of an Event of Default, and all expenses incurred in connection therewith (including reasonable fees and expenses of attorneys and other professionals) shall be for the sole account of Grantor and shall be chargeable (when due and payable); and

(iv) In no event shall Grantor, either itself or through any employee, licensee, or designee, file an application for the registration of any Patent, Trademark, or Copyright with the United States Patent and Trademark Office, the United States Copyright Office or any similar office or agency without giving Agent prior written notice thereof. Promptly upon any such Patent filing, Grantor shall comply with Section 6(g)(i) hereof and promptly after any other such filing, Grantor shall execute such additional documents as may be necessary to perfect Agent's Lien in such Trademarks and Copyrights, as applicable;

(h) Investment Related Property.

(i) If Grantor shall receive or become entitled to receive any Pledged Interests after the date hereof, it shall promptly (and in any event within 5 Business Days of receipt thereof) deliver to Agent a duly executed Pledged Interests Addendum identifying such Pledged Interests;

(ii) Upon and during the continuance of an Event of Default, all sums of money and property paid or distributed in respect of the Investment Related Property which are received by Grantor shall be held by Grantor in trust for the benefit of Agent segregated from Grantor's other property, and Grantor shall deliver it forthwith to Agent's in the exact form received;

(iii) Grantor shall promptly deliver to Agent a copy of each material notice or other communication received by it in respect of any Pledged Interests;

(iv) No Grantor shall make or consent to any amendment or other modification or waiver with respect to any Pledged Interests, Pledged Operating Agreement, or Pledged Partnership Agreement, or enter into any agreement or permit to exist any restriction with respect to any Pledged Interests other than pursuant to the Note Documents;

(v) Grantor agrees that it will cooperate with Agent in obtaining all necessary approvals and making all necessary filings under federal, state, local, or foreign law in connection with the Security Interest on the Investment Related Property or any sale or transfer thereof;

(vi) As to all limited liability company or partnership interests, issued under any Pledged Operating Agreement or Pledged Partnership Agreement, Grantor hereby represents, warrants and covenants that the Pledged Interests issued pursuant to such agreement (A) are not and shall not be dealt in or traded on securities exchanges or in securities markets, (B) do not and will not constitute investment company securities, and (C) are not and will not be held by Grantor in a securities account. In addition, none of the Pledged Operating Agreements, the Pledged Partnership Agreements, or any other agreements governing any of the Pledged Interests issued under any Pledged Operating Agreement or Pledged Partnership Agreement, provide or shall provide that such Pledged Interests are securities governed by Article 8 of the Uniform Commercial Code as in effect in any relevant jurisdiction;

(i) [Reserved].

(j) Transfers and Other Liens. Grantor shall not (i) sell, assign (by operation of law or otherwise) or otherwise dispose of, or grant any option with respect to, any of the Collateral, except in the ordinary course of business and consistent with past practice, or (ii) create or permit to exist any Lien upon or with respect to any of the Collateral of Grantor, except for Permitted Liens. The inclusion of Proceeds in the Collateral shall not be deemed to constitute Agent's consent to any sale or other disposition of any of the Collateral except as expressly permitted in this Agreement or the other Note Documents; and

(k) Other Actions as to Any and All Collateral. Grantor shall promptly (and in any event within 5 Business Days of acquiring or obtaining such Collateral) notify Agent in writing upon (i) acquiring or otherwise obtaining any Collateral after the date hereof consisting of Trademarks, Patents, Copyrights, Intellectual Property Licenses, Investment Related Property, Chattel Paper (electronic, tangible or otherwise), documents (as defined in Article 9 of the Code), promissory notes (as defined in the Code, or instruments (as defined in the Code) or (ii) any amount payable under or in connection with any of the Collateral being or becoming evidenced after the date hereof by any Chattel Paper, documents, promissory notes, or instruments, in each case with a value in excess of $10,000 individually and $25,000 in the aggregate and, in each such case upon the request of Agent, promptly execute such other documents, or if applicable, deliver such Chattel Paper, other

documents or certificates evidencing any Investment Related Property and do such other acts or things deemed necessary or desirable by Agent to protect Agent's Security Interest therein; and

(l) Changes in Locations, Names, etc. Grantor shall not, except upon prior written consent of Agent and delivery to Agent of additional financing statements and other documents reasonably requested by Agent as to the validity, perfection and priority of the Security Interests provided herein, change its name, identity, corporate structure or jurisdiction of organization.

(m) Notices. Grantor will advise Agent promptly, in reasonable detail, of: (i) any Lien (other than Permitted Liens) on any of the Collateral which would adversely affect the ability of Agent to exercise any of its remedies hereunder and (ii) the occurrence of any other event which could reasonably be expected to have a material adverse effect on the aggregate value of the Collateral.

7. Relation to Other Security Documents. The provisions of this Agreement shall be read and construed with the provisions of the Patent Security Agreements, which are supplemental to the provisions of this Agreement. Nothing contained in the Patent Security Agreements shall limit any of the rights or remedies of Agent hereunder.

8. Further Assurances.

(a) Grantor agrees that from time to time, at its own expense, Grantor will promptly execute and deliver all further instruments and documents, and take all further action, that may be necessary or that Agent may reasonably request, in order to perfect and protect the Security Interest granted or purported to be granted hereby or to enable Agent to exercise and enforce its rights and remedies hereunder with respect to any of the Collateral.

(b) Grantor authorizes the filing by Agent of financing or continuation statements, or amendments thereto, and Grantor will execute and deliver to Agent such other instruments or notices, as may be necessary or as Agent may reasonably request, in order to perfect and preserve the Security Interest granted or purported to be granted hereby.

(c) Grantor authorizes Agent at any time and from time to time to file, transmit, or communicate, as applicable, financing statements and amendments (i) describing the Collateral as "all personal property of debtor" or "all assets of debtor" or words of similar effect, (ii) describing the Collateral as being of equal or lesser scope or with greater detail, or (iii) that contain any information required by part 5 of Article 9 of the Code for the sufficiency or filing office acceptance. Grantor also hereby ratifies any and all financing statements or amendments previously filed by Agent in any jurisdiction.

(d) Grantor acknowledges that it is not authorized to file any financing statement or amendment or termination statement with respect to any financing statement

filed in connection with this Agreement without the prior written consent of Agent, subject to Grantor's rights under Section 9-509(d)(2) of the Code.

9. Agent's Right to Perform Contracts, Exercise Rights, etc. Upon the occurrence and during the continuance of an Event of Default, Agent (or its designee) (a) may proceed to perform any and all of the obligations of Grantor contained in any contract, lease, or other agreement and exercise any and all rights of Grantor therein contained as fully as Grantor itself could, (b) shall have the right to use Grantor's rights under Intellectual Property Licenses in connection with the enforcement of the Agent's rights hereunder, including the right to prepare for sale and sell any and all Inventory and Equipment now or hereafter owned by Grantor and now or hereafter covered by such licenses, and (c) shall have the right to request that any Stock that is pledged hereunder be registered in the name of Agent or any of its nominees.

10. Agent Appointed Attorney-in-Fact. Grantor hereby irrevocably appoints Agent its attorney-in-fact, with full authority in the place and stead of Grantor and in the name of Grantor or otherwise, at such time as an Event of Default has occurred and is continuing under the Notes, to take any action and to execute any instrument which Agent may reasonably deem necessary or advisable to accomplish the purposes of this Agreement, including:

(a) to ask, demand, collect, sue for, recover, compromise, receive and give acquittance and receipts for moneys due and to become due under or in connection with the Accounts or any other Collateral of Grantor;

(b) to receive and open all mail addressed to Grantor and to notify postal authorities to change the address for the delivery of mail to Grantor to that of Agent;

(c) to receive, indorse, and collect any drafts or other instruments, documents, Negotiable Collateral or Chattel Paper;

(d) to file any claims or take any action or institute any proceedings which Agent may deem necessary or desirable for the collection of any of the Collateral of Grantor or otherwise to enforce the rights of Agent with respect to any of the Collateral;

(e) to repair, alter, or supply goods, if any, necessary to fulfill in whole or in part the purchase order of any Person obligated to Grantor in respect of any Account of Grantor;

(f) to use any labels, Patents, Trademarks, trade names, URLs, domain names, industrial designs, Copyrights, advertising matter or other industrial or intellectual property rights, in advertising for sale and selling Inventory and other Collateral and to collect any amounts due under Accounts, contracts or Negotiable Collateral of Grantor; and

(g) Agent on behalf of the Purchaser Group shall have the right, but shall not be obligated, to bring suit in its own name to enforce the Trademarks, Patents,

Copyrights and Intellectual Property Licenses and, if Agent shall commence any such suit, the appropriate Grantor shall, at the request of Agent, do any and all lawful acts and execute any and all proper documents reasonably required by Agent in aid of such enforcement.

To the extent permitted by law, Grantor hereby ratifies all that such attorney-in-fact shall lawfully do or cause to be done by virtue hereof. This power of attorney is coupled with an interest and shall be irrevocable until this Agreement is terminated.

11. Appointment and Authorization of Agent. Each Purchaser hereby designates and appoints Agent as its representative under this Agreement and the other Note Documents and each Purchaser hereby irrevocably authorizes Agent to execute and deliver each of the other Note Documents on its behalf and to take such other action on its behalf under the provisions of this Agreement and each other Note Document and to exercise such powers and perform such duties as are expressly delegated to Agent by the terms of this Agreement or any other Note Document, together with such powers as are reasonably incidental thereto. Agent agrees to act as such on the express conditions contained in this Section 11. The provisions of this Section 11 are solely for the benefit of Agent and the Purchasers, and Debtor shall have no rights as a third party beneficiary of any of the provisions contained herein. Any provision to the contrary contained elsewhere in this Agreement or in any other Note Document notwithstanding, Agent shall not have any duties or responsibilities, except those expressly set forth herein, nor shall Agent have or be deemed to have any fiduciary relationship with any Purchaser, and no implied covenants, functions, responsibilities, duties, obligations or liabilities shall be read into this Agreement or any other Note Document or otherwise exist against Agent; it being expressly understood and agreed that the use of the word “Agent” is for convenience only, that Agent is merely the representative of the Purchasers, and only has the contractual duties set forth herein. Except as expressly otherwise provided in this Agreement, Agent shall have and may use its sole discretion with respect to exercising or refraining from exercising any discretionary rights or taking or refraining from taking any actions that Agent expressly is entitled to take or assert under or pursuant to this Agreement and the other Note Documents. Without limiting the generality of the foregoing, or of any other provision of the Note Documents that provides rights or powers to Agent, Purchasers agree that Agent shall have the right to exercise the following powers as long as this Agreement remains in effect: (a) maintain, in accordance with its customary business practices, ledgers and records reflecting the status of the Secured Obligations, the Collateral and related matters, (b) execute or file any and all financing or similar statements or notices, amendments, renewals, supplements, documents, instruments, proofs of claim, notices and other written agreements with respect to the Note Documents, (c) perform, exercise, and enforce any and all other rights and remedies of the Purchaser Group with respect to Debtor, the Secured Obligations, the Collateral, or otherwise related to any of same as provided in the Note Documents, and (d) incur and pay such Expenses as Agent may deem necessary or appropriate for the performance and fulfillment of its functions and powers pursuant to the Note Documents. Agent shall have no obligation whatsoever to any of the Purchasers to assure that the Collateral exists or is owned by Debtor or is cared for, protected, or insured or has been encumbered, or that the Agent’s Liens have been properly or sufficiently or lawfully created, perfected, protected, or enforced or are

entitled to any particular priority, or to exercise at all or in any particular manner or under any duty of care, disclosure or fidelity, or to continue exercising, any of the rights, authorities and powers granted or available to Agent pursuant to any of the Note Documents, it being understood and agreed that in respect of the Collateral, or any act, omission, or event related thereto, subject to the terms and conditions contained herein, Agent may act in any manner it may deem appropriate, in its sole discretion given Agent's own interest in the Collateral in its capacity as one of the Purchasers and that Agent shall have no other duty or liability whatsoever to any Purchaser as to any of the foregoing, except as otherwise provided herein.

12. Agent May Perform. If Grantor fails to perform any agreement contained herein and an Event of Default exists and is continuing, Agent may itself perform, or cause performance of, such agreement, and the reasonable expenses of Agent incurred in connection therewith shall be payable, jointly and severally, by Grantor.

13. Agent's Duties. The powers conferred on Agent hereunder are solely to protect the Purchasers' interest in the Collateral, for the benefit of the Purchaser Group, and shall not impose any duty upon Agent to exercise any such powers. Except for the safe custody of any Collateral in its actual possession and the accounting for moneys actually received by it hereunder, Agent shall have no duty as to any Collateral or as to the taking of any necessary steps to preserve rights against prior parties or any other rights pertaining to any Collateral. Agent shall be deemed to have exercised reasonable care in the custody and preservation of any Collateral in its actual possession if such Collateral is accorded treatment substantially equal to that which Agent accords its own property.

14. Collection of Accounts, General Intangibles and Negotiable Collateral. At any time upon the occurrence and during the continuation of an Event of Default, Agent or Agent's designee may (a) notify Account Debtors of Grantor that the Accounts, General Intangibles, Chattel Paper or Negotiable Collateral have been assigned to Agent, for the benefit of the Purchaser Group, or that Agent has a security interest therein, and (b) collect the Accounts, General Intangibles and Negotiable Collateral directly, and any collection costs and expenses shall constitute part of Grantor's Secured Obligations under the Note Documents.

15. Disposition of Pledged Interests by Agent. None of the Pledged Interests existing as of the date of this Agreement are, and none of the Pledged Interests hereafter acquired on the date of acquisition thereof will be, registered or qualified under the various federal or state securities laws of the United States and disposition thereof after an Event of Default may be restricted to one or more private (instead of public) sales in view of the lack of such registration. Grantor understands that in connection with such disposition, Agent may approach only a restricted number of potential purchasers and further understands that a sale under such circumstances may yield a lower price for the Pledged Interests than if the Pledged Interests were registered and qualified pursuant to federal and state securities laws and sold on the open market. Grantor, therefore, agrees that: (a) if Agent shall, pursuant to the terms of this Agreement, sell or cause the Pledged Interests or any portion thereof to be sold at a private sale, Agent shall have the right to rely upon the advice and

opinion of any nationally recognized brokerage or investment firm (but shall not be obligated to seek such advice and the failure to do so shall not be considered in determining the commercial reasonableness of such action) as to the best manner in which to offer the Pledged Interest or any portion thereof for sale and as to the best price reasonably obtainable at the private sale thereof; and (b) such reliance shall be conclusive evidence that Agent has handled the disposition in a commercially reasonable manner.

16. Voting Rights.

(a) Upon the occurrence and during the continuation of an Event of Default, (i) Agent may, at its option, and with two (2) Business Days prior notice to Grantor, and in addition to all rights and remedies available to Agent under any other agreement, at law, in equity, or otherwise, exercise all voting rights, and all other ownership or consensual rights in respect of the Pledged Interests owned by Grantor, but under no circumstances is Agent obligated by the terms of this Agreement to exercise such rights, and (ii) if Agent duly exercises its right to vote any of such Pledged Interests, Grantor hereby appoints Agent, Grantor's true and lawful attorney-in-fact and *irrevocable proxy* to vote such Pledged Interests in any manner Agent deems advisable for or against all matters submitted or which may be submitted to a vote of shareholders, partners or members, as the case may be. The power-of-attorney granted hereby is coupled with an interest and shall be irrevocable.

(b) For so long as Grantor shall have the right to vote the Pledged Interests owned by it, Grantor covenants and agrees that it will not, without the prior written consent of Agent, vote or take any consensual action with respect to such Pledged Interests which would materially adversely affect the rights of Agent and the other members of the Purchaser Group solely in connection with their rights as holders of the Notes (and not in connection with their rights solely as holders of Stock).

17. Remedies. Upon the occurrence and during the continuance of an Event of Default and upon the vote of the majority of holders of the Notes outstanding at such time:

(a) Agent may exercise in respect of the Collateral, in addition to other rights and remedies provided for herein, in the other Note Documents, or otherwise available to it, all the rights and remedies of a secured party on default under the Code or any other applicable law. Without limiting the generality of the foregoing, Grantor expressly agrees that, in any such event, Agent without demand of performance or other demand, advertisement or notice of any kind (except a notice specified below of time and place of public or private sale) to or upon Grantor or any other Person (all and each of which demands, advertisements and notices are hereby expressly waived to the maximum extent permitted by the Code or any other applicable law), may take immediate possession of all or any portion of the Collateral and (i) require Grantor to, and Grantor hereby agrees that it will at its own expense and upon the reasonable request of Agent forthwith, assemble all or part of the Collateral as directed by Agent and make it available to Agent at one or more locations where Grantor regularly maintains Inventory, and (ii) without notice except as specified

below, sell the Collateral or any part thereof in one or more parcels at public or private sale, at any of Agent's offices or elsewhere, for cash, on credit, and upon such other commercially reasonable terms as Agent may request. Grantor agrees that, to the extent notice of sale shall be required by law, at least 10 days notice to Grantor of the time and place of any public sale or the time after which any private sale is to be made shall constitute reasonable notification and specifically such notice shall constitute a reasonable "authenticated notification of disposition" within the meaning of Section 9-611 of the Code. Agent shall not be obligated to make any sale of Collateral regardless of notice of sale having been given. Agent may adjourn any public or private sale from time to time by announcement at the time and place fixed therefor, and such sale may, without further notice, be made at the time and place to which it was so adjourned.

(b) Agent is hereby granted a license or other right to use, other than any King George Property (solely during such time that the King George Property is subject to the lien described in the definition thereof), without liability for royalties or any other charge, Grantor's labels, Patents, Copyrights, rights of use of any name, trade secrets, trade names, Trademarks, service marks and advertising matter, URLs, domain names, industrial designs, other industrial or intellectual property or any property of a similar nature, whether owned by Grantor or with respect to which Grantor have rights under license, sublicense, or other agreements, as it pertains to the Collateral, in preparing for sale, advertising for sale and selling any Collateral, and Grantor's rights under all licenses and all franchise agreements shall inure to the benefit of Agent.

(c) Any cash held by Agent as Collateral and all cash proceeds received by Agent in respect of any sale of, collection from, or other realization upon all or any part of the Collateral shall be applied against the Notes and the Secured Obligations, *pari passu*. In the event the proceeds of Collateral are insufficient to satisfy all of the Secured Obligations in full, Grantor shall remain liable for any such deficiency.

(d) Grantor hereby acknowledges that the Secured Obligations arose out of a commercial transaction, and agrees that if an Event of Default shall occur and be continuing Agent shall have the right to an immediate writ of possession without notice of a hearing. Agent shall have the right upon notice to Grantor to the appointment of a receiver for the properties and assets of Grantor, and Grantor hereby consents to such rights and such appointment and hereby waives any objection Grantor may have thereto or the right to have a bond or other security posted by Agent.

18. Remedies Cumulative. Each right, power, and remedy of Agent as provided for in this Agreement or in the other Note Documents or now or hereafter existing at law or in equity or by statute or otherwise shall be cumulative and concurrent and shall be in addition to every other right, power, or remedy provided for in this Agreement or in the other Note Documents or now or hereafter existing at law or in equity or by statute or otherwise, and the exercise or beginning of the exercise by Agent, of any one or more of such rights, powers, or remedies shall not preclude the simultaneous or later exercise by Agent of any or all such other rights, powers, or remedies.

19. Marshaling. Agent shall not be required to marshal any present or future collateral security (including but not limited to the Collateral) for, or other assurances of payment of, the Secured Obligations or any of them or to resort to such collateral security or other assurances of payment in any particular order, and all of its rights and remedies hereunder and in respect of such collateral security and other assurances of payment shall be cumulative and in addition to all other rights and remedies, however existing or arising. To the extent that it lawfully may, Grantor hereby agrees that it will not invoke any law relating to the marshaling of collateral which might cause delay in or impede the enforcement of Agent's rights and remedies under this Agreement or under any other instrument creating or evidencing any of the Secured Obligations or under which any of the Secured Obligations is outstanding or by which any of the Secured Obligations is secured or payment thereof is otherwise assured, and, to the extent that it lawfully may, Grantor hereby irrevocably waives the benefits of all such laws.

20. Indemnity and Expenses.

(a) Grantor agrees to indemnify Agent and the other members of the Purchaser Group from and against all claims, lawsuits and liabilities (including reasonable attorneys fees) growing out of or resulting from this Agreement (including enforcement of this Agreement) or any other Note Document to which Grantor is a party, except claims, losses or liabilities resulting from the gross negligence or willful misconduct of the party seeking indemnification as determined by a final non-appealable order of a court of competent jurisdiction. This provision shall survive the termination of this Agreement and the repayment of the Secured Obligations.

(b) Grantor, jointly and severally, shall, upon demand, pay to Agent all the Expenses which Agent may incur in connection with (i) the administration of this Agreement, (ii) the custody, preservation, use or operation of, or, upon an Event of Default, the sale of, collection from, or other realization upon, any of the Collateral in accordance with this Agreement and the other Note Documents, (iii) the exercise or enforcement of any of the rights of Agent hereunder or (iv) the failure by Grantor to perform or observe any of the provisions hereof.

21. Merger, Amendments; Etc. THIS AGREEMENT, TOGETHER WITH THE OTHER NOTE DOCUMENTS, REPRESENTS THE FINAL AGREEMENT BETWEEN THE PARTIES AND MAY NOT BE CONTRADICTED BY EVIDENCE OF PRIOR, CONTEMPORANEOUS OR SUBSEQUENT ORAL AGREEMENTS OF THE PARTIES. THERE ARE NO UNWRITTEN AGREEMENTS BETWEEN THE PARTIES WITH RESPECT TO THE MATTERS PERTAINING TO THIS AGREEMENT. No waiver of any provision of this Agreement, and no consent to any departure by Grantor herefrom, shall in any event be effective unless the same shall be in writing and signed by Agent, and then such waiver or consent shall be effective only in the specific instance and for the specific purpose for which given. No amendment of any provision of this Agreement shall be effective unless the same shall be in writing and signed by Agent and Grantor to which such amendment applies.

22. Addresses for Notices. All notices and other communications provided for hereunder shall be given in the form and manner and delivered to Agent and to Grantor, at their respective addresses specified in the Securities Purchase Agreement, or, as to any party, at such other address as shall be designated by such party in a written notice to the other party.

23. Continuing Security Interest: Assignments under this Agreement. This Agreement shall create a continuing security interest in the Collateral and shall (a) remain in full force and effect until the Secured Obligations (other than inchoate indemnity obligations) have been paid in full in cash or redeemed or converted into Stock in accordance with the provisions of the Notes, (b) be binding upon Grantor and its successors and assigns, and (c) inure to the benefit of, and be enforceable by, Agent, and its successors, transferees and assigns. Without limiting the generality of the foregoing clause (c), each of Agent and the Purchasers may assign or otherwise transfer all or any portion of its rights and obligations under this Agreement to any other Person who receives transfer of any or all of the Notes as permitted under the Notes, and such other Person shall thereupon become vested with all the benefits in respect thereof granted to Agent herein or otherwise upon such person becoming a "Purchaser" pursuant to the terms of the Securities Purchase Agreement. Upon payment in full in cash or redemption or conversion of all the Secured Obligations (other than inchoate indemnity obligations) in accordance with the provisions of the Notes, the Security Interest granted hereby shall automatically terminate and all rights to the Collateral shall revert to Grantor or any other Person entitled thereto. At such time, Agent authorizes Debtor or any designee of Debtor to file appropriate termination statements or take any other steps that Debtor deems necessary to terminate such Security Interests. Except as provided herein, in the Securities Purchase Agreement or the Notes, no transfer or renewal, extension, assignment, or termination of this Agreement, any other Note Document, or any other instrument or document executed and delivered by Grantor to Agent nor any additional loans made by the Purchasers to Grantor, nor the taking of further security, nor the retaking or re-delivery of the Collateral to Grantor by Agent, nor any other act of the Purchaser Group, or any of them shall release Grantor from any obligation, except a release or discharge executed in writing by Agent. Agent shall not by any act, delay, omission or otherwise, be deemed to have waived any of its rights or remedies hereunder, unless such waiver is in writing and signed by Agent and then only to the extent therein set forth. A waiver by Agent of any right or remedy on any occasion shall not be construed as a bar to the exercise of any such right or remedy which Agent would otherwise have had on any other occasion.

24. Governing Law.

(a) **This Agreement shall be construed and enforced in accordance with, and all questions concerning the construction, validity, interpretation and performance of this Agreement shall be governed by, the internal laws of the State of California, without giving effect to any choice of law or conflict of law provision or rule (whether of the State of California or any other jurisdictions) that would cause the application of the laws of any jurisdictions other than the State of California.**

(b) THE PARTIES AGREE THAT ALL ACTIONS OR PROCEEDINGS ARISING IN CONNECTION WITH THIS AGREEMENT AND THE OTHER NOTE DOCUMENTS SHALL BE TRIED AND LITIGATED ONLY IN THE STATE AND, TO THE EXTENT PERMITTED BY APPLICABLE LAW, FEDERAL COURTS LOCATED IN THE CITY AND COUNTY OF SAN DIEGO, CALIFORNIA; PROVIDED, HOWEVER, THAT ANY SUIT SEEKING ENFORCEMENT AGAINST ANY COLLATERAL OR OTHER PROPERTY MAY BE BROUGHT, AT AGENT'S OPTION, IN THE COURTS OF ANY JURISDICTION WHERE AGENT ELECTS TO BRING SUCH ACTION OR WHERE SUCH COLLATERAL OR OTHER PROPERTY MAY BE FOUND. AGENT AND GRANTOR WAIVE, TO THE EXTENT PERMITTED UNDER APPLICABLE LAW, ANY RIGHT EACH MAY HAVE TO ASSERT THE DOCTRINE OF FORUM NON CONVENIENS OR TO OBJECT TO VENUE TO THE EXTENT ANY PROCEEDING IS BROUGHT IN SAN DIEGO, CALIFORNIA IN ACCORDANCE WITH THIS SECTION 24(b).

(c) TO THE MAXIMUM EXTENT PERMITTED BY APPLICABLE LAW, AGENT AND GRANTOR HEREBY WAIVE THEIR RESPECTIVE RIGHTS TO A JURY TRIAL OF ANY CLAIM OR CAUSE OF ACTION BASED UPON OR ARISING OUT OF THIS AGREEMENT OR ANY OF THE TRANSACTIONS CONTEMPLATED THEREIN, INCLUDING CONTRACT CLAIMS, TORT CLAIMS, BREACH OF DUTY CLAIMS, AND ALL OTHER COMMON LAW OR STATUTORY CLAIMS. AGENT AND GRANTOR REPRESENT THAT EACH HAS REVIEWED THIS WAIVER AND EACH KNOWINGLY AND VOLUNTARILY WAIVES ITS JURY TRIAL RIGHTS FOLLOWING CONSULTATION WITH LEGAL COUNSEL. IN THE EVENT OF LITIGATION, A COPY OF THIS AGREEMENT MAY BE FILED AS A WRITTEN CONSENT TO A TRIAL BY THE COURT.

25. Agent. Each reference herein to any right granted to, benefit conferred upon or power exercisable by the "Agent" shall be a reference to Agent, for the benefit of the Purchaser Group.

26. Miscellaneous.

(a) This Agreement may be executed in any number of counterparts and by different parties on separate counterparts, each of which, when executed and delivered, shall be deemed to be an original, and all of which, when taken together, shall constitute but one and the same Agreement. Delivery of an executed counterpart of this Agreement by telefacsimile or other electronic method of transmission shall be equally as effective as delivery of an original executed counterpart of this Agreement. Any party delivering an executed counterpart of this Agreement by telefacsimile or other electronic method of transmission also shall deliver an original executed counterpart of this Agreement but the failure to deliver an original executed counterpart shall not affect the validity, enforceability, and binding effect of this Agreement. The foregoing shall apply to each other Note Document *mutatis mutandis*.

(b) Any provision of this Agreement which is prohibited or unenforceable shall be ineffective to the extent of such prohibition or unenforceability without invalidating the remaining provisions hereof in that jurisdiction or affecting the validity or enforceability of such provision in any other jurisdiction.

(c) Headings used in this Agreement are for convenience only and shall not be used in connection with the interpretation of any provision hereof.

(d) The pronouns used herein shall include, when appropriate, either gender and both singular and plural, and the grammatical construction of sentences shall conform thereto.

(e) Unless the context of this Agreement or any other Note Document clearly requires otherwise, references to the plural include the singular, references to the singular include the plural, the terms "includes" and "including" are not limiting, and the term "or" has, except where otherwise indicated, the inclusive meaning represented by the phrase "and/or." The words "hereof," "herein," "hereby," "hereunder," and similar terms in this Agreement or any other Note Document refer to this Agreement or such other Note Document, as the case may be, as a whole and not to any particular provision of this Agreement or such other Note Document, as the case may be. Section, subsection, clause, schedule, and exhibit references herein are to this Agreement unless otherwise specified. Any reference in this Agreement or in any other Note Document to any agreement, instrument, or document shall include all alterations, amendments, changes, extensions, modifications, renewals, replacements, substitutions, joinders, and supplements, thereto and thereof, as applicable (subject to any restrictions on such alterations, amendments, changes, extensions, modifications, renewals, replacements, substitutions, joinders, and supplements set forth herein). Any reference herein or in any other Note Document to the satisfaction or repayment in full of the Secured Obligations shall mean the repayment in full in cash (or cash collateralization in accordance with the terms hereof) of all Secured Obligations other than unasserted contingent indemnification Secured Obligations. Any reference herein to any Person shall be construed to include such Person's successors and assigns. Any requirement of a writing contained herein or in any other Note Document shall be satisfied by the transmission of a Record and any Record so transmitted shall constitute a representation and warranty as to the accuracy and completeness of the information contained therein.

IN WITNESS WHEREOF, the undersigned parties hereto have executed this Agreement by and through their duly authorized officers, as of the day and year first above written.

GRANTOR:

A.P. PHARMA, INC.

By: /s/ John Whelan
Name: John Whelan
Title: Chief Executive Officer

AGENT:

TANG CAPITAL PARTNERS, LP

By: Tang Capital Management, LLC,
its general partner

By: /s/ Kevin Tang
Name: Kevin C. Tang
Title: Managing Director

PURCHASER:

TANG CAPITAL PARTNERS, LP

By: Tang Capital Management, LLC,
its general partner

By: /s/ Kevin Tang
Name: Kevin C. Tang
Title: Managing Director

PURCHASER: **BAKER BROS. INVESTMENTS II, L.P.**

By: Baker Bros. Capital, L.P.,
its general partner
By: Baker Bros. Capital (GP), LLC,
its general partner

By: /s/ Felix Baker
Name: Felix Baker
Title: Managing Member

PURCHASER: **BAKER BROTHERS LIFE SCIENCES, L.P.**

By: Baker Brothers Life Sciences Capital, L.P.,
its general partner
By: Baker Brothers Life Sciences Capital (GP), LLC,
its general partner

By: /s/ Felix Baker
Name: Felix Baker
Title: Managing Member

PURCHASER: **14159, L.P.**

By: 14159 Capital, L.P., its general partner
By: 14159 Capital (GP), LLC,
its general partner

By: /s/ Felix Baker
Name: Felix Baker
Title: Managing Member

EXHIBIT A

PATENT SECURITY AGREEMENT

This PATENT SECURITY AGREEMENT (this "Patent Security Agreement") is made this 24th day of April, 2011, among A.P. PHARMA, INC. ("Grantor"), and TANG CAPITAL PARTNERS, LP, in its capacity as representative for the Purchasers ("Agent").

RECITALS

WHEREAS, Pursuant to that certain Securities Purchase Agreement, dated as of April 24, 2011 (the "Securities Purchase Agreement"), by and among A.P. Pharma, Inc. ("Debtor"), Agent and Baker Bros. Investments II, L.P., Baker Brothers Life Sciences, L.P. and 14159, L.P., as Purchasers (collectively, the "Purchasers"), Debtor has agreed to issue to the Purchasers, and the Purchasers have agreed to purchase from Debtor, certain Secured Convertible Notes (the "Notes"), and

WHEREAS, the Purchasers are willing to make the financial accommodations to Debtor as provided for in the Securities Purchase Agreement and Notes, but only upon the condition, among others, that Grantor shall have executed and delivered to Agent, as representative of the Purchasers for the benefit of the Purchasers, that certain Security Agreement dated as of April 24, 2011 (including all annexes, exhibits or schedules thereto, as from time to time amended, restated, supplemented or otherwise modified, the "Security Agreement");

WHEREAS, pursuant to the Security Agreement, Grantor is required to execute and deliver to Agent this Patent Security Agreement;

NOW, THEREFORE, in consideration of the premises and mutual covenants herein contained and for other good and valuable consideration, the receipt and sufficiency of which are hereby acknowledged, Grantor hereby agrees as follows:

1. DEFINED TERMS. All capitalized terms used but not otherwise defined herein have the meanings given to them in the Security Agreement.

2. GRANT OF SECURITY INTEREST IN PATENT COLLATERAL. Grantor hereby grants to Agent a continuing first priority security interest in all of Grantor's right, title and interest in, to and under the following, whether presently existing or hereafter created or acquired (collectively, the "Patent Collateral"):

(a) all of its Patents and Patent Intellectual Property Licenses to which it is a party including those referred to on Schedule I hereto;

(b) all reissues, continuations or extensions of the foregoing; and

(c) all products and proceeds of the foregoing, including any claim by Grantor against third parties for past, present or future infringement or dilution of any Patent or any Patent licensed under any Intellectual Property License.

3. SECURITY FOR OBLIGATIONS. This Patent Security Agreement and the Security Interest created hereby secures the payment and performance of all the Secured Obligations, whether now existing or arising hereafter. Without limiting the generality of the foregoing, this Patent Security Agreement secures the payment of all amounts which constitute part of the Secured Obligations and would be owed by Grantor, or any of them, to Agent, whether or not they are unenforceable or not allowable due to the existence of an Insolvency Proceeding involving Grantor.

4. SECURITY AGREEMENT. The security interests granted pursuant to this Patent Security Agreement are granted in conjunction with the security interests granted to Agent pursuant to the Security Agreement. Grantor hereby acknowledges and affirms that the rights and remedies of Agent with respect to the security interest in the Patent Collateral made and granted hereby are more fully set forth in the Security Agreement, the terms and provisions of which are incorporated by reference herein as if fully set forth herein.

5. AUTHORIZATION TO SUPPLEMENT. If Grantor shall obtain rights to any new patentable inventions or become entitled to the benefit of any patent application or patent for any reissue, division, or continuation, of any patent, the provisions of this Patent Security Agreement shall automatically apply thereto. Grantor shall give prompt notice in writing to Agent with respect to any such new patent rights. Without limiting Grantor's obligations under this Section 5, Grantor hereby authorizes Agent unilaterally to modify this Agreement by amending Schedule I to include any such new patent rights of Grantor. Notwithstanding the foregoing, no failure to so modify this Patent Security Agreement or amend Schedule I shall in any way affect, invalidate or detract from Agent's continuing security interest in all Collateral, whether or not listed on Schedule I.

6. COUNTERPARTS. This Patent Security Agreement may be executed in any number of counterparts, each of which shall be deemed to be an original, but all such separate counterparts shall together constitute but one and the same instrument. In proving this Patent Security Agreement or any other Note Document in any judicial proceedings, it shall not be necessary to produce or account for more than one such counterpart signed by the party against whom such enforcement is sought. Any signatures delivered by a party by facsimile transmission or by e-mail transmission shall be deemed an original signature hereto.

7. CONSTRUCTION. Unless the context of this Patent Security Agreement or any other Note Document clearly requires otherwise, references to the plural include the singular, references to the singular include the plural, the terms "includes" and "including" are not limiting, and the term "or" has, except where otherwise indicated, the inclusive meaning represented by the phrase "and/or." The words "hereof," "herein," "hereby," "hereunder," and similar terms in this Patent Security Agreement or any other

Note Document refer to this Patent Security Agreement or such other Note Document, as the case may be, as a whole and not to any particular provision of this Patent Security Agreement or such other Note Document, as the case may be. Section, subsection, clause, schedule, and exhibit references herein are to this Patent Security Agreement unless otherwise specified. Any reference in this Patent Security Agreement or in any other Note Document to any agreement, instrument, or document shall include all alterations, amendments, changes, extensions, modifications, renewals, replacements, substitutions, joinders, and supplements, thereto and thereof, as applicable (subject to any restrictions on such alterations, amendments, changes, extensions, modifications, renewals, replacements, substitutions, joinders, and supplements set forth herein). Any reference herein or in any other Note Document to the satisfaction or repayment in full of the Secured Obligations shall mean the repayment in full in cash (or cash collateralization in accordance with the terms hereof) of all Obligations other than unasserted contingent indemnification Secured Obligations. Any reference herein to any Person shall be construed to include such Person's successors and assigns. Any requirement of a writing contained herein or in any other Note Document shall be satisfied by the transmission of a Record and any Record so transmitted shall constitute a representation and warranty as to the accuracy and completeness of the information contained therein.

[signature page follows]

IN WITNESS WHEREOF, Grantor has caused this Patent Security Agreement to be executed and delivered by its duly authorized officer as of the date first set forth above.

A.P. PHARMA, INC.

By: _____
Name: _____
Title: _____

ACCEPTED AND ACKNOWLEDGED BY:

TANG CAPITAL PARTNERS, LP, as Agent

By: Tang Capital Management, LLC,
its general partner

By: _____
Name: Kevin C. Tang
Title: Managing Director

EXHIBIT B

ANNEX 1 TO PLEDGE AND SECURITY AGREEMENT

Pledged Interests Addendum

This Pledged Interests Addendum, dated as of _____ __, 2011, is delivered pursuant to Section 6 of the Security Agreement referred to below. The undersigned hereby agrees that this Pledged Interests Addendum may be attached to that certain Security Agreement, dated as of April 24, 2011 (as amended, restated, supplemented or otherwise modified from time to time, the "Security Agreement"), made by the undersigned to Tang Capital Partners, LP, in its capacity as Agent. Initially capitalized terms used but not defined herein shall have the meaning ascribed to such terms in the Security Agreement. The undersigned hereby agrees that the additional interests listed on this Pledged Interests Addendum as set forth below shall be and become part of the Pledged Interests pledged by the undersigned to Agent in the Security Agreement and any pledged company set forth on this Pledged Interests Addendum as set forth below shall be and become a "Pledged Company" under the Security Agreement, each with the same force and effect as if originally named therein.

The undersigned hereby certifies that the representations and warranties set forth in Section 4 of the Security Agreement of the undersigned are true and correct as to the Pledged Interests listed herein on and as of the date hereof.

A.P. PHARMA, INC.

By: _____
Name: _____
Title: _____

Name of Pledgor	Name of Pledged Company	Number of Shares/Units	Class of Interests	Percentage of Class Owned	Certificate Nos.

Exhibit 10.4

SECOND AMENDMENT TO LEASE

This Second Amendment to Lease ("Amendment") is entered into as of April 1, 2011 (the "Effective Date") by and between METROPOLITAN LIFE INSURANCE COMPANY, a New York corporation ("Landlord"), and AP PHARMA, INC., a Delaware corporation ("Tenant"), with reference to the following facts ("Recitals"):

A. Landlord and Tenant are the current parties to that certain Lease dated as of November 7, 1997 executed by Landlord and Tenant's predecessor-in-interest, Advanced Polymer Systems, as amended by that certain Amendment to Lease Agreement dated as of March 29, 2004 executed by Landlord and Tenant (collectively, the "Existing Lease") for certain Premises described therein commonly known as 123 Saginaw Drive, Redwood City, California 94063, all as more particularly described in the Existing Lease. The Expiration Date under the Existing Lease is currently March 31, 2011.

B. Tenant and Landlord desire to provide for the extension of the Term and other amendments of the Existing Lease, but only in strict accordance with and as more particularly set forth in this Amendment.

NOW, THEREFORE, in consideration of the foregoing, and of the mutual covenants set forth herein and of other good and valuable consideration, the receipt and adequacy of which are hereby acknowledged, the parties hereto agree as follows:

Section 1. Scope of Amendment; Defined Terms. Except as expressly provided in this Amendment, the Existing Lease shall remain in full force and effect. Should any inconsistency arise between this Amendment and the Existing Lease as to the specific matters which are the subject of this Amendment, the terms and conditions of this Amendment shall control. The term "Lease" as used herein and, from and after the Effective Date, in the Existing Lease shall refer to the Existing Lease as modified by this Amendment. Unless otherwise indicated, capitalized terms used in this Amendment shall be defined as set forth in the Lease. Landlord and Tenant agree that this Amendment shall be effective as of the Effective Date with the same force and effect as if executed on that date.

Section 2. Conditions Precedent. Concurrently with Tenant's execution and delivery of this Amendment to Landlord, Tenant shall satisfy all of the following (the "Conditions Precedent"): (i) Tenant shall pay to Landlord One Hundred Ten Thousand Two Hundred Nine Dollars and Seventy-Four Cents ($110,209.74) to be applied toward Basic Annual Rent and Additional Rent with respect to April 2011 and May 2011; and (ii) Tenant shall deposit with Landlord Fifty-Five Thousand One Hundred Four Dollars and Eighty-Seven Cents ($55,104.87) to be held as the Security Deposit. If all Conditions Precedent are not fully satisfied or waived in writing by Landlord in its sole discretion, Sections 3, 4 and 5 of this Amendment shall be null and void *ab initio*, and of no force or effect in any respect whatsoever at any time.

Section 3. Amended Amount of Security Deposit. Notwithstanding any provision of the Existing Lease to the contrary, from and after the Effective Date the Security Deposit shall be cash in the amount of Fifty-Five Thousand One Hundred Four Dollars and Eighty-Seven Cents ($55,104.87).

Section 4. Extension of Term. Notwithstanding any provision of the Existing Lease to the contrary, the Expiration Date is hereby extended to be September 30, 2011 (the period from April 1, 2011 through September 30, 2011 is referred to herein as the "Second Extended Term"). This extension is with respect to the entire Premises and this extension is further upon and subject to the same conditions, terms, covenants and agreements contained in the Existing Lease except as otherwise provided in this Amendment. Landlord and Tenant acknowledge and agree that this Amendment provides all rights and obligations of the parties with respect to extension of the current Term, whether or not in accordance with any other provisions, if any, of the Existing Lease or otherwise regarding renewal or extension, and any such provisions, options or rights for renewal or extension are hereby deleted as of the Effective Date.

Section 5. Basic Annual Rent. Notwithstanding any provision of the Existing Lease to the contrary, Basic Annual Rent and Monthly Installments thereof shall continue to be due and payable by Tenant with respect to the Second Extended Term in the same manner required under the Lease therefor in the following amounts:

Period From/To	Monthly Installments
April 1, 2011 – September 30, 2011	$41,967.87 (total for six months = $251,807.22)

Section 6. Condition of Premises. Notwithstanding any provision of the Existing Lease to the contrary, Tenant acknowledges and agrees that: (1) Tenant has been in occupancy of the Premises since 1997; (2) Tenant has investigated the condition of the Premises to the extent Tenant desires to do so; (3) Tenant is leasing the Premises in its "As Is" condition; (4) no representation regarding the condition of the Premises has been made by or on behalf of Landlord; and (5) in connection with this Amendment, Landlord has no obligation to remodel or to make any repairs, alterations or improvements in connection with this Amendment, or to provide Tenant any allowance therefor.

Section 7. Change of Address for Copies of Notices to Landlord. The current addresses for notices to be sent to Landlord pursuant to Paragraph 23 of the Existing Lease are modified as follows:

Metropolitan Life Insurance Company
c/o Seaport Centre Property Manager
701 Chesapeake Drive
Redwood City, California 94063
Attention: Property Manager

with copies to the following:

Metropolitan Life Insurance Company
425 Market Street, Suite 1050
San Francisco, California 94105
Attention: EIM Manager, Real Estate Investments

and

Metropolitan Life Insurance Company
425 Market Street, Suite 1050
San Francisco, California 94105
Attention: Associate General Counsel

Section 8. Time of Essence. Without limiting the generality of any other provision of the Existing Lease, time is of the essence to each and every term and condition of this Amendment.

Section 9. Brokers. Tenant represents that no broker, agent or person has represented, dealt with or had discussions with it in connection with this Amendment transaction other than Kristoph Lodge of Cornish & Carey Commercial ("Landlord's Broker") and that no broker, agent or person except Landlord's Broker has brought about this Amendment transaction. Tenant hereby indemnifies and agrees to protect, defend and hold Landlord harmless from and against all claims, losses, damages, liability, costs and expenses (including, without limitation, attorneys' fees and expenses) by any broker, agent or other person (except Landlord's Broker) claiming a commission or other form of compensation by virtue of alleged representation of, or dealings or discussions with, Tenant with respect to the transaction contemplated by this Amendment. Tenant shall not be responsible for payment of any commission to Landlord's Broker. The provisions of this Section shall survive the expiration or earlier termination of the Amendment or the Lease.

Section 10. Attorneys' Fees. Each party to this Amendment shall bear its own attorneys' fees and costs incurred in connection with the discussions preceding, negotiations for and documentation of this Amendment. In the event any party brings any suit or other proceeding with respect to the subject matter or enforcement of this Amendment or the Lease, the prevailing party (as determined by the court, agency or other authority before which such suit or proceeding is commenced) shall, in addition to such other relief as may be awarded, be entitled to recover attorneys' fees, expenses and costs of investigation as actually incurred, including court costs,

expert witness fees, costs and expenses of investigation, and all attorneys' fees, costs and expenses in any such suit or proceeding (including in any action or participation in or in connection with any case or proceeding under the Bankruptcy Code, 11 United States Code Sections 101 et seq., or any successor statutes, in establishing or enforcing the right to indemnification, in appellate proceedings, or in connection with the enforcement or collection of any judgment obtained in any such suit or proceeding).

Section 11. Effect of Headings. The titles or headings of the various parts or sections hereof are intended solely for convenience and are not intended and shall not be deemed to or in any way be used to modify, explain or place any construction upon any of the provisions of this Amendment.

Section 12. Entire Agreement; Amendment. This Amendment taken together with the Existing Lease, together with all exhibits, schedules, riders and addenda to each, constitutes the full and complete agreement and understanding between the parties hereto and shall supersede all prior communications, representations, understandings or agreements, if any, whether oral or written, concerning the subject matter contained in this Amendment and the Existing Lease, as so amended, and no provision of the Lease as so amended may be modified, amended, waived or discharged, in whole or in part, except by a written instrument executed by all of the parties hereto.

Section 13. OFAC. Landlord advises Tenant hereby that the purpose of this Section is to provide to the Landlord information and assurances to enable Landlord to comply with the law relating to OFAC.

Tenant hereby represents, warrants and covenants to Landlord, either that (i) Tenant is regulated by the SEC, FINRA or the Federal Reserve (a "Regulated Entity") or (ii) neither Tenant nor any person or entity that directly or indirectly (a) controls Tenant or (b) has an ownership interest in Tenant of twenty-five percent (25%) or more, appears on the list of Specially Designated Nationals and Blocked Persons ("OFAC List") published by the Office of Foreign Assets Control ("OFAC") of the U.S. Department of the Treasury.

If, in connection with the Lease, there is one or more Guarantors of Tenant's obligations under the Lease, then Tenant further represents, warrants and covenants either that (i) any such Guarantor is a Regulated Entity or (ii) neither Guarantor nor any person or entity that directly or indirectly (a) controls such Guarantor or (b) has an ownership interest in such Guarantor of twenty-five percent (25%) or more, appears on the OFAC List.

Tenant covenants during the term of the Lease to provide to Landlord information reasonably requested by Landlord, including, without limitation, organizational structural charts and organizational documents, which Landlord may deem to be necessary ("Tenant OFAC Information") in order for Landlord to confirm Tenant's continuing compliance with the provisions of this Section. Tenant represents and warrants that the Tenant OFAC Information it has provided or to be provided to Landlord or Landlord's Broker in connection with the execution of this Amendment is true and complete.

Section 14. Ratification. Tenant represents to Landlord as of the Effective Date that: (a) the Existing Lease is in full force and effect and has not been modified except as provided by this Amendment; (b) there are no defaults or unfulfilled obligations on the part of Landlord under the Lease; and (c) Tenant is currently in possession of the entire Premises and neither the Premises, nor any part thereof, is occupied by any subtenant or other party other than Tenant.

Section 15. Authority. Each person executing this Amendment represents and warrants that he or she is duly authorized and empowered to execute it, and does so as the act of and on behalf of the party indicated below.

Section 16. Counterparts. This Amendment may be executed in duplicates or counterparts, or both, and such duplicates or counterparts together shall constitute but one original of the Amendment. The parties contemplate that they may be executing counterparts of this Amendment transmitted by facsimile and agree and intend that a signature by facsimile machine shall bind the party so signing with the same effect as though the signature were an original signature. Each duplicate and counterpart shall be equally admissible in evidence, and each original shall fully bind each party who has executed it.

IN WITNESS WHEREOF, the parties hereto have executed this Amendment as of the Effective Date.

TENANT: **AP PHARMA, INC.,**
a Delaware corporation

By: /s/ John Whelan
Print Name: John Whelan
Title: President, Chief Executive Officer

LANDLORD: **METROPOLITAN LIFE INSURANCE COMPANY,**
a New York corporation

By: /s/ Greg Hill
Print Name: Greg Hill
Title: Director

Exhibit 10.5

A.P. PHARMA, INC.

MANAGEMENT RETENTION AGREEMENT

This Management Retention Agreement (the "Agreement") is dated as of April 25, 2011, by and between John B. Whelan ("Employee") and A.P. Pharma, Inc., a Delaware corporation (the "Company"). This Agreement is intended to provide Employee with certain benefits described herein upon the occurrence of specific events.

RECITALS

A. The Company's Board of Directors believes it is in the best interests of the Company and its shareholders to retain Employee and provide incentives to Employee to continue in the service of the Company.

B. The Board of Directors further believes that it is imperative to provide Employee with certain benefits upon Employee's Involuntary Termination or a Change of Control, which benefits are intended to provide Employee with financial security and provide sufficient income and encouragement to Employee to remain employed with the Company, notwithstanding the possibility of a Change of Control.

D. To accomplish the foregoing objectives, the Board of Directors has directed the Company, upon execution of this Agreement by Employee, to agree to the terms provided in this Agreement.

It is therefore agreed as follows:

1. **At-Will Employment**. The Company and Employee acknowledge that Employee's employment is and shall continue to be at-will, as defined under applicable law, and that Employee's employment with the Company may be terminated by either party at any time for any or no reason. If Employee's employment terminates for any reason, Employee shall not be entitled to any payments, benefits, damages, award or compensation other than as provided in this Agreement or otherwise agreed to by the Company. The terms of this Agreement shall terminate upon the earlier of: (i) the date on which Employee ceases to be employed as a corporate officer of the Company, other than as a result of an Involuntary Termination; or (ii) the date that all obligations of the parties hereunder have been satisfied. A termination of the terms of this Agreement pursuant to the preceding sentence shall be effective for all purposes, except that such termination shall not affect the payment or provision of compensation or benefits on account of a termination of employment occurring prior to the termination of the terms of this Agreement. The rights and duties created by this Section 1 are contingent upon Employee's release of claims against the Company (at the time of termination in a form reasonably satisfactory to the Company) and may not be modified in any way except by a written agreement executed by an officer of the Company upon direction from the Board of Directors.

2. **Benefits Upon Termination of Employment.**

(a) **Severance Upon Involuntary Termination.** In the event that Employee suffers an Involuntary Termination at any time under circumstances other than as covered in paragraph 2(b) below, then in addition to all salary and bonuses accrued as of the date of Employee's termination of employment, Employee will be entitled to receive severance benefits as follows: (i) during the period commencing on the date of Employee's termination and ending on the date twelve (12) months after the effective date of the termination (the "Severance Period") the Company shall pay to Employee an amount equal to the monthly base salary which Employee was receiving immediately prior to the Involuntary Termination in accordance with the Company's standard payroll practices; (ii) the average bonus paid by the Company to Employee for services during each of the three 12- month periods (or such shorter period of time during which Employee was eligible for a bonus) prior to the Involuntary Termination date, which payments shall be paid during the Severance Period in accordance with the Company's standard payroll practices; and (iii) reimbursement for or continuation of payment by the Company of its portion of the health insurance benefits provided to Employee immediately prior to the Involuntary Termination pursuant to the terms of the Consolidated Omnibus Budget Reconciliation Act of 1985, as amended ("COBRA") or other applicable law through the earlier of the end of the Severance Period or the date upon which Employee is no longer eligible for such COBRA or other benefits under applicable law. In addition, Employee's stock options, restricted stock and other equity awards shall immediately vest, become exercisable and/or the restrictions thereon lapse with respect to that number of shares of Company common stock that otherwise would have vested during the Severance Period had Employee's employment continued. Employee's stock options, restricted stock and other equity awards shall otherwise be subject to the terms of the plan and option or award agreement pursuant to which such options and other equity awards were granted.

(b) **Severance Upon a Change in Control.** In the event that Employee suffers an Involuntary Termination within the twelve (12) month period following the effective date of a Change of Control, then in addition to all salary and bonuses accrued as of the date of Employee's termination of employment, Employee will be entitled to receive severance benefits as follows: (i) during the period commencing on the date of Employee's termination and ending on the date eighteen (18) months after the effective date of the termination (the "Change of Control Severance Period") the Company shall pay to Employee an amount equal to the greater of (A) the monthly base salary which Employee was receiving immediately prior to the Involuntary Termination or (B) the monthly base salary which Employee was receiving immediately prior to the Change of Control, in each case, in accordance with the Company's standard payroll practices; (ii) one hundred and fifty percent (150%) of the average bonus paid by the Company to Employee for services during each of the three 12- month periods (or such shorter period of time during which Employee was eligible for a bonus) prior to the Involuntary Termination date, which payments shall be paid during the Change of Control Severance Period in accordance with the Company's standard payroll practices; and (iii) reimbursement for or continuation of payment by the Company of its portion of the health insurance benefits provided to Employee immediately prior to the Involuntary Termination pursuant to the terms of COBRA or other applicable law through the earlier of the end of the Change of Control Severance Period

or the date upon which Employee is no longer eligible for such COBRA or other benefits under applicable law. In addition, Employee's stock options, restricted stock and other equity awards shall immediately vest, become exercisable and/or the restrictions thereon lapse with respect to one hundred percent (100%) of the shares of Company common stock subject thereto. Employee's stock options, restricted stock and other equity awards shall otherwise be subject to the terms of the plan and option or award agreement pursuant to which such options and other equity awards were granted.

(c) **Termination for Cause**. Notwithstanding any other provision of this Agreement, if Employee's employment is terminated for Cause at any time, then Employee shall not be entitled to receive payment of any severance benefits or any continuation or acceleration of stock option vesting or relinquishment of forfeiture and transfer restrictions on restricted stock awards. Employee will receive payment(s) for all salary and bonuses accrued as of the date of Employee's termination of employment.

(d) **Voluntary Resignation**. If Employee voluntarily resigns from the Company under circumstances which do not constitute an Involuntary Termination, then Employee shall not be entitled to receive payment of any severance benefits, or option acceleration, or relinquishment of forfeiture and transfer restrictions. Employee will receive payment(s) for all salary and bonuses accrued as of the date of Employee's termination of employment.

3. **Definition of Terms**. The following terms referred to in this Agreement shall have the following meanings:

(a) **"Cause"** means any of the following: (i) Employee's theft, dishonesty, willful misconduct, breach of fiduciary duty for personal profit, or falsification of any Company or Affiliate documents or records; (ii) Employee's material failure to abide by a Company's or Affiliate's code of conduct or other policies (including without limitation, policies relating to confidentiality and reasonable workplace conduct); (iii) Employee's unauthorized use, misappropriation, destruction or diversion of any tangible or intangible asset or corporate opportunity of the Company or an Affiliate (including, without limitation, Employee's improper use or disclosure of confidential or proprietary information); (iv) any intentional act by Employee which has a material detrimental effect on the Company or an Affiliate's reputation or business; (v) Employee's repeated failure or inability to perform any reasonable assigned duties after written notice from the Company or an Affiliate (including, without limitation, habitual absence from work for reasons other than illness), and a reasonable opportunity to cure, such failure or inability; (vi) any material breach by Employee of any employment or service agreement between Employee and the Company or an Affiliate, which breach is not cured pursuant to the terms of such agreement; or (vii) Employee's conviction (including any plea of guilty or *nolo contendere*) of any criminal act involving fraud, dishonesty, misappropriation or moral turpitude, or which impairs Employee's ability to perform his or her duties with the Company or an Affiliate.

(b) **"Change in Control"** means the occurrence of any of the following:

(i) an Ownership Change Event or a series of related Ownership Change Events (collectively, a "**Transaction**") in which the stockholders of the Company immediately before the Transaction do not retain immediately after the Transaction, in substantially the same proportions as their ownership of shares of the Company's voting stock immediately before the Transaction, direct or indirect beneficial ownership of more than fifty percent (50%) of the total combined voting power of the outstanding voting securities of the Company or such surviving entity immediately outstanding after the Transaction, or, in the case of an Ownership Change Event the entity to which the assets of the Company were transferred (the "**Transferee**"), as the case may be; or

(ii) the liquidation or dissolution of the Company.

For purposes of the preceding sentence, indirect beneficial ownership shall include, without limitation, an interest resulting from ownership of the voting securities of one or more corporations or other business entities which own the Company or the Transferee, as the case may be, either directly or through one or more subsidiary corporations or other business entities. The Board shall have the right to determine whether multiple sales or exchanges of the voting securities in the Company or multiple Ownership Change Events are related, and its determination shall be final, binding and conclusive. The Board may also, but need not, specify that other transactions or events constitute a Change in Control.

(c) **"Involuntary Termination"** shall include any termination by the Company other than for Cause and Employee's voluntary termination within sixty days following the occurrence of any of the following events without Employee's written consent: (i) a material reduction or change in job duties, responsibilities and requirements inconsistent with Employee's position with the Company and Employee's prior duties, responsibilities and requirements or a material negative change in Employee's reporting relationship; (ii) a material reduction of Employee's base compensation (other than in connection with a general decrease in base salaries for most officers of the Company or successor corporation); or (iii) Employee's refusal to relocate to a facility or location more than forty miles from the Company's current location, provided that Employee will not resign due to such change, reduction or relocation without first providing the Company with written notice of the event or events constituting the grounds for his voluntary resignation within thirty days of the initial existence of such grounds and a reasonable cure period of not less than thirty days following the date of such notice.

(d) **"Ownership Change Event"** means the occurrence of any of the following with respect to the Company: (i) the direct or indirect sale or exchange in a single or series of related transactions by the stockholders of the Company of more than fifty percent (50%) of the voting stock of the Company; (ii) a merger or consolidation in which the Company is a party; or (iii) the sale, exchange, or transfer of all or substantially all of the assets of the Company.

4. **Limitation and Conditions on Payments.**

(a) **Parachute Payments**. In the event that the severance and other benefits provided for in this Agreement to the Employee: (i) constitute "parachute payments" within the meaning of Section 280G of the Internal Revenue Code of 1986, as amended (the "Code"); and (ii) but for this Section, would be subject to the excise tax imposed by Section 4999 of the Code, then the Employee's severance benefits under Sections 2(a) and 2(b) shall be payable either:

(i) in full; or

(ii) as to such lesser amount which would result in no portion of such severance benefits being subject to excise tax under Section 4999 of the Code, whichever of the foregoing amounts, taking into account the applicable federal, state and local income taxes and the excise tax imposed by Section 4999, results in the receipt by the Employee on an after-tax basis, of the greatest amount of severance benefits under Section 2(a) and 2(b), notwithstanding that all or some portion of such severance benefits may be taxable under Section 4999 of the Code. Any determination required under this Section 4 shall be made in writing by independent public accountants selected by the Company (the "Accountants"), whose determination shall be conclusive and binding upon the Employee and the Company for all purposes. For purposes of making the calculations required by this Section 4, the Accountants may make reasonable assumptions and approximations concerning applicable taxes and may rely on reasonable, good faith interpretations concerning the application of Section 280G and 4999 of the Code. The Company and the Employee shall furnish to the Accountants such information and documents as the Accountants may reasonably request in order to make a determination under this Section. The Company shall bear all costs the Accountants may reasonably incur in connection with any calculations contemplated by this Section 4. Any reduction in severance benefits required by this Section 4 shall occur in a manner necessary to provide the service provider with the greatest economic benefit. If more than one manner of reduction of severance benefits necessary to arrive at the reduced amount yields the greatest economic benefit to the service provider, the payments and benefits shall be reduced pro rata.

(b) **Release Prior to Receipt of Benefits**. Prior to the receipt of any benefits under this Agreement, Employee shall execute and allow to become effective, a release of claims agreement in a form acceptable to the Company (the "Release") not later than fifty-two (52) days following Employee's employment termination in the form provided by the Company. Such Release shall specifically relate to all of Employee's rights and claims in existence at the time of such execution and shall confirm Employee's obligations under the Company's standard form of proprietary information agreement. In no event will severance benefits be provided to Employee until the Release becomes effective. In the event severance payments are delayed because of the effective date of the Release, the Company will pay Employee the severance payments, that Employee would otherwise have received under Section 2(a) on or prior to the effective date of the Release, on the first regular payroll pay day following the effective date of the release, with the balance of the payments being paid as originally scheduled.

5. **Section 409A**. All severance payments to be made upon a termination of employment under this Agreement may be made only upon a "separation of service" within the meaning of Section 409A of the Code and the Department of Treasury regulations and other guidance promulgated thereunder. Notwithstanding any provision to the contrary in this Agreement, if Employee is deemed by the Company at the time of Employee's separation from service to be a "specified employee" for purposes of Code Section 401A(a)(2)(B)(i), to the extent delayed commencement of any portion of the benefits to which Employee is entitled under this Agreement is required in order to avoid a prohibited distribution under Code Section 409A(a)(2)(B)(i), such portion of Employee's benefits shall not be provided to Employee prior to the earlier of (i) the expiration of the six-month period measured from the date of Employee's "separation of service" with the Company or (ii) the date of Employee's death. Upon the first business day following the expiration of the applicable Code Section 409A(a)(2)(B)(i) period, all payments deferred pursuant to this Section 5 shall be paid in a lump sum to Employee, and any remaining payments due under the Agreement shall be paid as otherwise provided herein. For purposes of Code Section 409A (including, without limitation, for purposes of Treasury Regulation Section 1.409A-2(b)(2)(iii)), Employee's right to receive installment payments under this Agreement shall be treated as a right to receive a series of separate payments and, accordingly, each installment payment hereunder shall at all times be considered a separate and distinct payment. It is intended that none of the severance payments and benefits to be provided hereunder will be subject to Section 409A of the Code and any ambiguities herein will be interpreted to be so exempt. Employee and the Company agree to work together in good faith to consider amendments to this Agreement and to take such reasonable actions which are necessary, appropriate or desirable to avoid imposition of any additional tax or income recognition prior to actual payment to Employee under Section 409A of the Code. Notwithstanding anything to the contrary contained herein, to the extent that any amendment to this Agreement with respect to the payment of any severance payments or benefits would constitute under Code Section 409A a delay in a payment or a change in the form of payment, then such amendment must be done in a manner that complies with Code Section 409A(a)(4)(C).

6. **Conflicts**. Employee represents that Employee's performance of all the terms of this Agreement will not breach any other agreement to which Employee is a party. Employee has not, and will not during the term of this Agreement, enter into any oral or written agreement in conflict with any of the provisions of this Agreement. Employee further represents that Employee is entering into or has entered into an employment relationship with the Company of Employee's own free will and that Employee has not been solicited as an employee in any way by the Company.

7. **Successors**. Any successor to the Company (whether direct or indirect and whether by purchase, lease, merger, consolidation, liquidation or otherwise) to all or substantially all of the Company's business and/or assets shall assume the obligations under this Agreement and agree expressly to perform the obligations under this Agreement in the same manner and to the same extent as the Company would be required to perform such obligations in the absence of a succession. The terms of this Agreement and all of Employee's rights hereunder and thereunder shall inure to the benefit of, and be enforceable by, Employee's personal or legal representatives, executors, administrators, successors, heirs, distributees, devisees and legatees.

8. **Notice**. Notices and all other communications contemplated by this Agreement shall be in writing and shall be deemed to have been duly given when personally delivered or when mailed by U.S. registered or certified mail, return receipt requested and postage prepaid. Mailed notices to Employee shall be addressed to Employee at the home address which Employee most recently communicated to the Company in writing. In the case of the Company, mailed notices shall be addressed to its corporate headquarters, and all notices shall be directed to the attention of its Secretary.

9. **Miscellaneous Provisions**.

(a) **No Duty to Mitigate**. Employee shall not be required to mitigate the amount of any payment contemplated by this Agreement (whether by seeking new employment or in any other manner), nor shall any such payment be reduced by any earnings that Employee may receive from any other source.

(b) **Waiver**. No provision of this Agreement shall be modified, waived or discharged unless the modification, waiver or discharge is agreed to in writing and signed by Employee and by an authorized officer of the Company (other than Employee). No waiver by either party of any breach of, or of compliance with, any condition or provision of this Agreement by the other party shall be considered a waiver of any other condition or provision or of the same condition or provision at another time.

(c) **Whole Agreement**. No agreements, representations or understandings (whether oral or written and whether express or implied) which are not expressly set forth in this Agreement have been made or entered into by either party with respect to the subject matter hereof. This Agreement supersedes any agreement of the same title and concerning similar subject matter dated prior to the Effective Date, and by execution of this Agreement both parties agree that any such predecessor agreement shall be deemed null and void.

(d) **Choice of Law**. The validity, interpretation, construction and performance of this Agreement shall be governed by the laws of the State of California without reference to conflict of laws provisions.

(e) **Severability**. If any term or provision of this Agreement or the application thereof to any circumstance shall, in any jurisdiction and to any extent, be invalid or unenforceable, such term or provision shall be ineffective as to such jurisdiction to the extent of such invalidity or unenforceability without invalidating or rendering unenforceable the remaining terms and provisions of this Agreement or the application of such terms and provisions to circumstances other than those as to which it is held invalid or unenforceable, and a suitable and equitable term or provision shall be substituted therefore to carry out, insofar as may be valid and enforceable, the intent and purpose of the invalid or unenforceable term or provision.

(f) **Arbitration**. Any dispute or controversy arising under or in connection with this Agreement may be settled at the option of either party by binding arbitration in the County of San Mateo, California, in accordance with the rules of the American Arbitration

Association then in effect. Judgment may be entered on the arbitrator's award in any court having jurisdiction. Punitive damages shall not be awarded.

(g) **Legal Fees and Expenses**. The parties shall each bear their own expenses, legal fees and other fees incurred in connection with this Agreement.

(h) **No Assignment of Benefits**. The rights of any person to payments or benefits under this Agreement shall not be made subject to option or assignment, either by voluntary or involuntary assignment or by operation of law, including (without limitation) bankruptcy, garnishment, attachment or other creditor's process, and any action in violation of this Section 9(h) shall be void.

(i) **Employment Taxes**. All payments made pursuant to this Agreement will be subject to withholding of applicable income and employment taxes.

(j) **Assignment by Company**. The Company may assign its rights under this Agreement to an affiliate, and an affiliate may assign its rights under this Agreement to another affiliate of the Company or to the Company. In the case of any such assignment, the term "Company" when used in a section of this Agreement shall mean the corporation that actually employs the Employee.

(k) **Counterparts**. This Agreement may be executed in counterparts, each of which shall be deemed an original, but all of which together will constitute one and the same instrument.

(l) **Renewal**. This Agreement shall remain in effect until December 31, 2011 and shall be automatically renewed for additional one year periods unless not later than three months prior to December 31st of any year either party gives written notice to the other party of the intention to terminate the Agreement effective December 31st of that year, provided, that in no event shall this Agreement terminate during the twelve (12) month period commencing upon a Change of Control.

[Signature page follows]

The parties have executed this Agreement on the date first written above.

A.P. PHARMA, INC.

By: /s/ Paul Goddard
Name: Paul Goddard, Ph.D.
Title: Chairman

EMPLOYEE

Signature: /s/ John Whelan
John B. Whelan

Address:

Exhibit 10.6

A.P. PHARMA, INC.

MANAGEMENT RETENTION AGREEMENT

This Management Retention Agreement (the "Agreement") is dated as of April 25, 2011, by and between Michael A. Adam, Ph.D. ("Employee") and A.P. Pharma, Inc., a Delaware corporation (the "Company"). This Agreement is intended to provide Employee with certain benefits described herein upon the occurrence of specific events.

RECITALS

A. The Company's Board of Directors believes it is in the best interests of the Company and its shareholders to retain Employee and provide incentives to Employee to continue in the service of the Company.

B. The Board of Directors further believes that it is imperative to provide Employee with certain benefits upon Employee's Involuntary Termination or a Change of Control, which benefits are intended to provide Employee with financial security and provide sufficient income and encouragement to Employee to remain employed with the Company, notwithstanding the possibility of a Change of Control.

D. To accomplish the foregoing objectives, the Board of Directors has directed the Company, upon execution of this Agreement by Employee, to agree to the terms provided in this Agreement.

It is therefore agreed as follows:

1. **At-Will Employment**. The Company and Employee acknowledge that Employee's employment is and shall continue to be at-will, as defined under applicable law, and that Employee's employment with the Company may be terminated by either party at any time for any or no reason. If Employee's employment terminates for any reason, Employee shall not be entitled to any payments, benefits, damages, award or compensation other than as provided in this Agreement or otherwise agreed to by the Company. The terms of this Agreement shall terminate upon the earlier of: (i) the date on which Employee ceases to be employed as a corporate officer of the Company, other than as a result of an Involuntary Termination; or (ii) the date that all obligations of the parties hereunder have been satisfied. A termination of the terms of this Agreement pursuant to the preceding sentence shall be effective for all purposes, except that such termination shall not affect the payment or provision of compensation or benefits on account of a termination of employment occurring prior to the termination of the terms of this Agreement. The rights and duties created by this Section 1 are contingent upon Employee's release of claims against the Company (at the time of termination in a form reasonably satisfactory to the Company) and may not be modified in any way except by a written agreement executed by an officer of the Company upon direction from the Board of Directors.

2. **Benefits Upon Termination of Employment.**

(a) **Severance Upon Involuntary Termination.** In the event that Employee suffers an Involuntary Termination at any time under circumstances other than as covered in paragraph 2(b) below, then in addition to all salary and bonuses accrued as of the date of Employee's termination of employment, Employee will be entitled to receive severance benefits as follows: (i) during the period commencing on the date of Employee's termination and ending on the date six (6) months after the effective date of the termination (the "Severance Period") the Company shall pay to Employee an amount equal to the monthly base salary which Employee was receiving immediately prior to the Involuntary Termination in accordance with the Company's standard payroll practices; (ii) one-half the average bonus paid by the Company to Employee for services during each of the three 12- month periods (or such shorter period of time during which Employee was eligible for a bonus) prior to the Involuntary Termination date, which payments shall be paid during the Severance Period in accordance with the Company's standard payroll practices; and (iii) reimbursement for or continuation of payment by the Company of its portion of the health insurance benefits provided to Employee immediately prior to the Involuntary Termination pursuant to the terms of the Consolidated Omnibus Budget Reconciliation Act of 1985, as amended ("COBRA") or other applicable law through the earlier of the end of the Severance Period or the date upon which Employee is no longer eligible for such COBRA or other benefits under applicable law. In addition, Employee's stock options, restricted stock and other equity awards shall immediately vest, become exercisable and/or the restrictions thereon lapse with respect to that number of shares of Company common stock that otherwise would have vested during the Severance Period had Employee's employment continued. Employee's stock options, restricted stock and other equity awards shall otherwise be subject to the terms of the plan and option or award agreement pursuant to which such options and other equity awards were granted.

(b) **Severance Upon a Change in Control.** In the event that Employee suffers an Involuntary Termination within the twelve (12) month period following the effective date of a Change of Control, then in addition to all salary and bonuses accrued as of the date of Employee's termination of employment, Employee will be entitled to receive severance benefits as follows: (i) during the period commencing on the date of Employee's termination and ending on the date twelve (12) months after the effective date of the termination (the "Change of Control Severance Period") the Company shall pay to Employee an amount equal to the greater of (A) the monthly base salary which Employee was receiving immediately prior to the Involuntary Termination or (B) the monthly base salary which Employee was receiving immediately prior to the Change of Control, in each case, in accordance with the Company's standard payroll practices; (ii) the average bonus paid by the Company to Employee for services during each of the three 12- month periods (or such shorter period of time during which Employee was eligible for a bonus) prior to the Involuntary Termination date, which payments shall be paid during the Change of Control Severance Period in accordance with the Company's standard payroll practices; and (iii) reimbursement for or continuation of payment by the Company of its portion of the health insurance benefits provided to Employee immediately prior to the Involuntary Termination pursuant to the terms of COBRA or other applicable law through the earlier of the end of the Change of Control Severance Period or the date upon which Employee is no longer

eligible for such COBRA or other benefits under applicable law. In addition, Employee's stock options, restricted stock and other equity awards shall immediately vest, become exercisable and/or the restrictions thereon lapse with respect to one hundred percent (100%) of the shares of Company common stock subject thereto. Employee's stock options, restricted stock and other equity awards shall otherwise be subject to the terms of the plan and option or award agreement pursuant to which such options and other equity awards were granted.

(c) **Termination for Cause**. Notwithstanding any other provision of this Agreement, if Employee's employment is terminated for Cause at any time, then Employee shall not be entitled to receive payment of any severance benefits or any continuation or acceleration of stock option vesting or relinquishment of forfeiture and transfer restrictions on restricted stock awards. Employee will receive payment(s) for all salary and bonuses accrued as of the date of Employee's termination of employment.

(d) **Voluntary Resignation**. If Employee voluntarily resigns from the Company under circumstances which do not constitute an Involuntary Termination, then Employee shall not be entitled to receive payment of any severance benefits, or option acceleration, or relinquishment of forfeiture and transfer restrictions. Employee will receive payment(s) for all salary and bonuses accrued as of the date of Employee's termination of employment.

3. **Definition of Terms**. The following terms referred to in this Agreement shall have the following meanings:

(a) **"Cause"** means any of the following: (i) Employee's theft, dishonesty, willful misconduct, breach of fiduciary duty for personal profit, or falsification of any Company or Affiliate documents or records; (ii) Employee's material failure to abide by a Company's or Affiliate's code of conduct or other policies (including without limitation, policies relating to confidentiality and reasonable workplace conduct); (iii) Employee's unauthorized use, misappropriation, destruction or diversion of any tangible or intangible asset or corporate opportunity of the Company or an Affiliate (including, without limitation, Employee's improper use or disclosure of confidential or proprietary information); (iv) any intentional act by Employee which has a material detrimental effect on the Company or an Affiliate's reputation or business; (v) Employee's repeated failure or inability to perform any reasonable assigned duties after written notice from the Company or an Affiliate (including, without limitation, habitual absence from work for reasons other than illness), and a reasonable opportunity to cure, such failure or inability; (vi) any material breach by Employee of any employment or service agreement between Employee and the Company or an Affiliate, which breach is not cured pursuant to the terms of such agreement; or (vii) Employee's conviction (including any plea of guilty or *nolo contendere*) of any criminal act involving fraud, dishonesty, misappropriation or moral turpitude, or which impairs Employee's ability to perform his or her duties with the Company or an Affiliate.

(b) **"Change in Control"** means the occurrence of any of the following:

(i) an Ownership Change Event or a series of related Ownership Change Events (collectively, a "**Transaction**") in which the stockholders of the Company

immediately before the Transaction do not retain immediately after the Transaction, in substantially the same proportions as their ownership of shares of the Company's voting stock immediately before the Transaction, direct or indirect beneficial ownership of more than fifty percent (50%) of the total combined voting power of the outstanding voting securities of the Company or such surviving entity immediately outstanding after the Transaction, or, in the case of an Ownership Change Event the entity to which the assets of the Company were transferred (the "**Transferee**"), as the case may be; or

(ii) the liquidation or dissolution of the Company.

For purposes of the preceding sentence, indirect beneficial ownership shall include, without limitation, an interest resulting from ownership of the voting securities of one or more corporations or other business entities which own the Company or the Transferee, as the case may be, either directly or through one or more subsidiary corporations or other business entities. The Board shall have the right to determine whether multiple sales or exchanges of the voting securities in the Company or multiple Ownership Change Events are related, and its determination shall be final, binding and conclusive. The Board may also, but need not, specify that other transactions or events constitute a Change in Control.

(c) **"Involuntary Termination"** shall include any termination by the Company other than for Cause and Employee's voluntary termination within sixty days following the occurrence of any of the following events without Employee's written consent: (i) a material reduction or change in job duties, responsibilities and requirements inconsistent with Employee's position with the Company and Employee's prior duties, responsibilities and requirements or a material negative change in Employee's reporting relationship; (ii) a material reduction of Employee's base compensation (other than in connection with a general decrease in base salaries for most officers of the Company or successor corporation); or (iii) Employee's refusal to relocate to a facility or location more than forty miles from the Company's current location, provided that Employee will not resign due to such change, reduction or relocation without first providing the Company with written notice of the event or events constituting the grounds for his voluntary resignation within thirty days of the initial existence of such grounds and a reasonable cure period of not less than thirty days following the date of such notice.

(d) "**Ownership Change Event**" means the occurrence of any of the following with respect to the Company: (i) the direct or indirect sale or exchange in a single or series of related transactions by the stockholders of the Company of more than fifty percent (50%) of the voting stock of the Company; (ii) a merger or consolidation in which the Company is a party; or (iii) the sale, exchange, or transfer of all or substantially all of the assets of the Company.

4. **Limitation and Conditions on Payments.**

(a) **Parachute Payments**. In the event that the severance and other benefits provided for in this Agreement to the Employee: (i) constitute "parachute payments" within the meaning of Section 280G of the Internal Revenue Code of 1986, as amended (the "Code"); and (ii) but for this Section, would be subject to the excise tax imposed by Section 4999 of the Code, then the Employee's severance benefits under Sections 2(a) and 2(b) shall be payable either:

(i) in full; or

(ii) as to such lesser amount which would result in no portion of such severance benefits being subject to excise tax under Section 4999 of the Code, whichever of the foregoing amounts, taking into account the applicable federal, state and local income taxes and the excise tax imposed by Section 4999, results in the receipt by the Employee on an after-tax basis, of the greatest amount of severance benefits under Section 2(a) and 2(b), notwithstanding that all or some portion of such severance benefits may be taxable under Section 4999 of the Code. Any determination required under this Section 4 shall be made in writing by independent public accountants selected by the Company (the "Accountants"), whose determination shall be conclusive and binding upon the Employee and the Company for all purposes. For purposes of making the calculations required by this Section 4, the Accountants may make reasonable assumptions and approximations concerning applicable taxes and may rely on reasonable, good faith interpretations concerning the application of Section 280G and 4999 of the Code. The Company and the Employee shall furnish to the Accountants such information and documents as the Accountants may reasonably request in order to make a determination under this Section. The Company shall bear all costs the Accountants may reasonably incur in connection with any calculations contemplated by this Section 4. Any reduction in severance benefits required by this Section 4 shall occur in a manner necessary to provide the service provider with the greatest economic benefit. If more than one manner of reduction of severance benefits necessary to arrive at the reduced amount yields the greatest economic benefit to the service provider, the payments and benefits shall be reduced pro rata.

(b) **Release Prior to Receipt of Benefits**. Prior to the receipt of any benefits under this Agreement, Employee shall execute and allow to become effective, a release of claims agreement in a form acceptable to the Company (the "Release") not later than fifty-two (52) days following Employee's employment termination in the form provided by the Company. Such Release shall specifically relate to all of Employee's rights and claims in existence at the time of such execution and shall confirm Employee's obligations under the Company's standard form of proprietary information agreement. In no event will severance benefits be provided to Employee until the Release becomes effective. In the event severance payments are delayed because of the effective date of the Release, the Company will pay Employee the severance payments, that Employee would otherwise have received under Section 2(a) on or prior to the effective date of the Release, on the first regular payroll pay day following the effective date of the release, with the balance of the payments being paid as originally scheduled.

5. **Section 409A**. All severance payments to be made upon a termination of employment under this Agreement may be made only upon a "separation of service" within the meaning of Section 409A of the Code and the Department of Treasury regulations and other guidance promulgated thereunder. Notwithstanding any provision to the contrary in this Agreement, if Employee is deemed by the Company at the time of Employee's separation from service to be a "specified employee" for purposes of Code Section 401A(a)(2)(B)(i), to the extent delayed commencement of any portion of the benefits to which Employee is entitled under this Agreement is required in order to avoid a prohibited distribution under Code Section 409A(a)(2)(B)(i), such portion of Employee's benefits shall not be provided to Employee prior to the earlier of (i) the expiration of the six-month period measured from the date of Employee's "separation of service" with the Company or (ii) the date of Employee's death. Upon the first business day following the expiration of the applicable Code Section 409A(a)(2)(B)(i) period, all payments deferred pursuant to this Section 5 shall be paid in a lump sum to Employee, and any remaining payments due under the Agreement shall be paid as otherwise provided herein. For purposes of Code Section 409A (including, without limitation, for purposes of Treasury Regulation Section 1.409A-2(b)(2)(iii)), Employee's right to receive installment payments under this Agreement shall be treated as a right to receive a series of separate payments and, accordingly, each installment payment hereunder shall at all times be considered a separate and distinct payment. It is intended that none of the severance payments and benefits to be provided hereunder will be subject to Section 409A of the Code and any ambiguities herein will be interpreted to be so exempt. Employee and the Company agree to work together in good faith to consider amendments to this Agreement and to take such reasonable actions which are necessary, appropriate or desirable to avoid imposition of any additional tax or income recognition prior to actual payment to Employee under Section 409A of the Code. Notwithstanding anything to the contrary contained herein, to the extent that any amendment to this Agreement with respect to the payment of any severance payments or benefits would constitute under Code Section 409A a delay in a payment or a change in the form of payment, then such amendment must be done in a manner that complies with Code Section 409A(a)(4)(C).

6. **Conflicts**. Employee represents that Employee's performance of all the terms of this Agreement will not breach any other agreement to which Employee is a party. Employee has not, and will not during the term of this Agreement, enter into any oral or written agreement in conflict with any of the provisions of this Agreement. Employee further represents that Employee is entering into or has entered into an employment relationship with the Company of Employee's own free will and that Employee has not been solicited as an employee in any way by the Company.

7. **Successors**. Any successor to the Company (whether direct or indirect and whether by purchase, lease, merger, consolidation, liquidation or otherwise) to all or substantially all of the Company's business and/or assets shall assume the obligations under this Agreement and agree expressly to perform the obligations under this Agreement in the same manner and to the same extent as the Company would be required to perform such obligations in the absence of a succession. The terms of this Agreement and all of Employee's rights hereunder and thereunder shall inure to the benefit of, and be enforceable by, Employee's personal or legal representatives, executors, administrators, successors, heirs, distributees, devisees and legatees.

8. **Notice**. Notices and all other communications contemplated by this Agreement shall be in writing and shall be deemed to have been duly given when personally delivered or when mailed by U.S. registered or certified mail, return receipt requested and postage prepaid. Mailed notices to Employee shall be addressed to Employee at the home address which Employee most recently communicated to the Company in writing. In the case of the Company, mailed notices shall be addressed to its corporate headquarters, and all notices shall be directed to the attention of its Secretary.

9. **Miscellaneous Provisions**.

(a) **No Duty to Mitigate**. Employee shall not be required to mitigate the amount of any payment contemplated by this Agreement (whether by seeking new employment or in any other manner), nor shall any such payment be reduced by any earnings that Employee may receive from any other source.

(b) **Waiver**. No provision of this Agreement shall be modified, waived or discharged unless the modification, waiver or discharge is agreed to in writing and signed by Employee and by an authorized officer of the Company (other than Employee). No waiver by either party of any breach of, or of compliance with, any condition or provision of this Agreement by the other party shall be considered a waiver of any other condition or provision or of the same condition or provision at another time.

(c) **Whole Agreement**. No agreements, representations or understandings (whether oral or written and whether express or implied) which are not expressly set forth in this Agreement have been made or entered into by either party with respect to the subject matter hereof. This Agreement supersedes any agreement of the same title and concerning similar subject matter dated prior to the Effective Date, and by execution of this Agreement both parties agree that any such predecessor agreement shall be deemed null and void.

(d) **Choice of Law**. The validity, interpretation, construction and performance of this Agreement shall be governed by the laws of the State of California without reference to conflict of laws provisions.

(e) **Severability**. If any term or provision of this Agreement or the application thereof to any circumstance shall, in any jurisdiction and to any extent, be invalid or unenforceable, such term or provision shall be ineffective as to such jurisdiction to the extent of such invalidity or unenforceability without invalidating or rendering unenforceable the remaining terms and provisions of this Agreement or the application of such terms and provisions to circumstances other than those as to which it is held invalid or unenforceable, and a suitable and equitable term or provision shall be substituted therefore to carry out, insofar as may be valid and enforceable, the intent and purpose of the invalid or unenforceable term or provision.

(f) **Arbitration**. Any dispute or controversy arising under or in connection with this Agreement may be settled at the option of either party by binding arbitration in the County of San Mateo, California, in accordance with the rules of the American Arbitration

Association then in effect. Judgment may be entered on the arbitrator's award in any court having jurisdiction. Punitive damages shall not be awarded.

(g) **Legal Fees and Expenses**. The parties shall each bear their own expenses, legal fees and other fees incurred in connection with this Agreement.

(h) **No Assignment of Benefits**. The rights of any person to payments or benefits under this Agreement shall not be made subject to option or assignment, either by voluntary or involuntary assignment or by operation of law, including (without limitation) bankruptcy, garnishment, attachment or other creditor's process, and any action in violation of this Section 9(h) shall be void.

(i) **Employment Taxes**. All payments made pursuant to this Agreement will be subject to withholding of applicable income and employment taxes.

(j) **Assignment by Company**. The Company may assign its rights under this Agreement to an affiliate, and an affiliate may assign its rights under this Agreement to another affiliate of the Company or to the Company. In the case of any such assignment, the term "Company" when used in a section of this Agreement shall mean the corporation that actually employs the Employee.

(k) **Counterparts**. This Agreement may be executed in counterparts, each of which shall be deemed an original, but all of which together will constitute one and the same instrument.

(l) **Renewal**. This Agreement shall remain in effect until December 31, 2011 and shall be automatically renewed for additional one year periods unless not later than three months prior to December 31st of any year either party gives written notice to the other party of the intention to terminate the Agreement effective December 31st of that year, provided, that in no event shall this Agreement terminate during the twelve (12) month period commencing upon a Change of Control.

[Signature page follows]

The parties have executed this Agreement on the date first written above.

A.P. PHARMA, INC.

By: /s/ John Whelan
Name: John B. Whelan
Title: President & CEO

EMPLOYEE

Signature: /s/ Michael A. Adam
Michael A. Adam, Ph.D.

Address:

Exhibit 99.1

For Immediate Release

A.P. Pharma Announces Financing of Up to $4.5 Million and Names CEO and COO

REDWOOD CITY, Calif. – April 25, 2011 – A.P. Pharma, Inc. (OTCQB: APPA), a specialty pharmaceutical company, today announced that it has entered into definitive agreements with investors, including Tang Capital Partners, LP, for a private placement of up to $4.5 million in convertible notes. The transaction is expected to close on or about April 29, 2011, subject to the satisfaction of certain closing conditions. Upon the closing, an initial amount of $1.5 million will be funded to the Company. Proceeds from the financing will be used to achieve important milestones toward resubmitting the APF530 New Drug Application (NDA) to the U.S. Food and Drug Administration (FDA).

The Company also announced that it has appointed John B. Whelan as president, chief executive officer and a director and Michael A. Adam, Ph.D. as senior vice president and chief operating officer.

“Since taking the position of acting chief executive officer, John has helped the organization move forward in an efficient manner to address the concerns expressed by the FDA in its Complete Response Letter regarding the NDA for our lead product, APF530,” said Paul Goddard, Ph.D., chairman of A.P. Pharma’s board of directors. “Under John’s leadership, the Company has held productive meetings with the FDA and gained agreement on the proposed resolution to some of the issues identified in the Complete Response Letter. As a result of this progress, we were able to secure bridge financing and attract Dr. Michael Adam, who brings over 25 years of experience in drug development, regulatory affairs and pharmaceutical operations, as our chief operating officer.”

Summary of Terms of the Financing

The $4.5 million of convertible notes issuable pursuant to this transaction have a 10-year term and will be convertible into shares of A.P. Pharma common stock at a conversion rate of 25,000 shares of common stock for every $1,000 of principal that is converted. The convertible notes bear an annual interest rate of 20%, payable quarterly in cash or via addition to the principal amount of the convertible notes at the election of the investors. The initial proceeds from this transaction are $1.5 million. The remaining $3.0 million can be funded to the Company at the investors’ discretion within two years of the closing date. Additional terms of this transaction will be disclosed on a Form 8-K Report to be filed by the Company with the Securities and Exchange Commission.

This press release is not an offer to sell or the solicitation of an offer to buy any securities of the Company, nor shall there be any sales of the securities in any jurisdiction in which such offer, solicitation, or sale would be unlawful prior to the

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registration or qualification under the securities laws of any such jurisdiction. The securities were offered only to accredited investors. The securities referenced herein have not been registered under the Securities Act of 1933, as amended, or any state securities laws, and may not be offered or sold in the United States absent registration or an applicable exemption from registration requirements.

The Company anticipates having to seek additional debt or equity financing or evaluate strategic alternatives. Multiple factors, including the Company's progress towards its NDA resubmission and market conditions, may prevent the Company from obtaining adequate financing to support its operations, or obtaining financing that will be on terms favorable to A.P. Pharma or its stockholders.

Management Changes

The Company has appointed John B. Whelan as president, chief executive officer and a director. Mr. Whelan has been with A.P. Pharma since February 2009, serving most recently as acting chief executive officer and chief financial officer and previously as vice president of finance and chief financial officer. Prior to joining A.P. Pharma, Mr. Whelan was chief operating officer and chief financial officer at Raven biotechnologies, Inc., where he oversaw the finance function and had broad operational responsibilities.

In addition, Michael A. Adam, Ph.D., has joined A.P. Pharma as senior vice president and chief operating officer. Dr. Adam has been working with the Company as a consultant since July 2010 and brings over 25 years of drug development and pharmaceutical operations experience to the organization. He was most recently senior vice president of pharmaceutical operations at Spectrum Pharmaceuticals, Inc., where he oversaw CMC development, quality assurance and manufacturing. Prior to Spectrum, Dr. Adam served as vice president, drug development operations at Anadys Pharmaceuticals, Inc., where he was responsible for regulatory affairs, quality assurance, pharmaceutical development, manufacturing and project management. He also has held senior positions with Pfizer, Inc., Agouron Pharmaceuticals, Inc. and Bristol-Myers Squibb Company. Dr. Adam earned his Ph.D. in Organic Chemistry at the Massachusetts Institute of Technology.

"Michael has an impressive track record in drug development, regulatory affairs and pharmaceutical operations," Dr. Goddard continued. "Over the past nine months, Michael has played a vital role as a consultant to A.P. Pharma in helping the Company address some of the FDA's questions surrounding the NDA for APF530. We look forward to his continued contributions as we progress toward our NDA resubmission."

About APF530

A.P. Pharma's lead product, APF530, prevents both acute-onset and delayed-onset chemotherapy-induced nausea and vomiting. APF530 contains the 5-HT_3 antagonist, granisetron, formulated in the Company's proprietary Biochronomer™ drug delivery system, which allows therapeutic drug levels to be maintained for five days with a single subcutaneous injection. Granisetron was selected because it is widely prescribed by physicians based on a well-established record of safety and efficacy.

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About A.P. Pharma

A.P. Pharma is a specialty pharmaceutical company developing products using its proprietary Biochronomer™ polymer-based drug delivery technology. The Company's primary focus is on its lead product, APF530, for the prevention of CINV. A.P. Pharma received a Complete Response Letter on the APF530 NDA and is targeting the resubmission of the NDA for the first half of 2012. The Company has additional clinical and preclinical stage programs in the area of pain management, all of which utilize its bioerodible injectable and implantable delivery systems. Further work on these programs has been deferred while the Company focuses on the approval of APF530. For further information, please visit the Company's web site at www.appharma.com.

Forward-looking Statements

This news release contains "forward-looking statements" as defined by the Private Securities Litigation Reform Act of 1995. These forward-looking statements involve risks and uncertainties, including uncertainties associated with capital resources and liquidity, timely development and regulatory approval of product candidates, satisfactory completion of clinical studies, progress in research and development programs, launch and acceptance of new products and other risks and uncertainties identified in the Company's filings with the Securities and Exchange Commission. We caution investors that forward-looking statements reflect our analysis only on their stated date. We do not intend to update them except as required by law.

Contacts

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