SUNAIR SERVICES CORP
Form 10-Q
May 15, 2008

Table of Contents

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549
FORM 10-Q

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

For the quarterly period ended March 31, 2008

OR

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

For the transition period from to

Commission file number I-4334
SUNAIR SERVICES CORPORATION
(Exact name of Registrant as specified in its charter)

Florida	59-0780772
(State or other jurisdiction of incorporation or organization)	*(I.R.S. Employer Identification No.)*
595 South Federal Highway, Suite 500 Boca Raton, Florida	33432
(Address of principal executive offices)	*(Zip Code)*

(561) 208-7400
(Registrant s telephone number, including area code)
None

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

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes þ No o

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

Large accelerated filer o	Accelerated filer o	Non-accelerated filer o (Do not check if a smaller reporting company)	Smaller reporting company þ

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes o No þ

As of 4/30/08, the Registrant had 13,091,088 shares outstanding of common stock.

SUNAIR SERVICES CORPORATION AND SUBSIDIARIES
INDEX

EX-31.1 Section 302 Certification of CEO
EX-31.2 Section 302 Certification of CFO
EX-32.1 Section 906 Certification of CEO
EX-32.2 Section 906 Certification of CFO

Table of Contents

PART I
FINANCIAL INFORMATION

Item 1. ***Financial Statements***

SUNAIR SERVICES CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS
AS OF MARCH 31, 2008 AND SEPTEMBER 30, 2007
(UNAUDITED)

	March 31, 2008	September 30, 2007
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	$ 3,276,604	$ 2,781,838
Accounts receivable, net	4,768,613	3,481,064
Inventories, net	2,060,048	1,826,636
Prepaid and other current assets	1,762,752	2,185,909
Total Current Assets	11,868,017	10,275,447
PROPERTY, PLANT, AND EQUIPMENT, net	2,029,081	2,118,552
OTHER ASSETS:		
Note receivable	2,000,000	2,000,000
Software costs, net	271,104	359,375
Customer list, net	9,318,905	10,958,234
Goodwill	62,112,528	60,675,353
Other assets	409,103	390,294
Total Other Assets	74,111,640	74,383,256
TOTAL ASSETS	$ 88,008,738	$ 86,777,255

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements.

Table of Contents

SUNAIR SERVICES CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS
AS OF MARCH 31, 2008 AND SEPTEMBER 30, 2007
(UNAUDITED)

	March 31, 2008	September 30, 2007
LIABILITIES AND STOCKHOLDERS EQUITY		
CURRENT LIABILITIES:		
Accounts payable	$ 2,191,722	$ 2,346,395
Accrued expenses	3,917,539	4,263,674
Unearned revenues	1,003,036	952,417
Customer deposits	3,562,953	3,166,264
Notes payable and capital leases, current portion	1,838,327	409,029
Total Current Liabilities	12,513,577	11,137,779
LONG TERM LIABILITIES:		
Notes payable and capital leases, net of current portion	4,635,520	5,545,456
Note payable -related party	5,000,000	5,000,000
Revolving line of credit	10,532,796	6,732,796
Total Long Term Liabilities	20,168,316	17,278,252
TOTAL LIABILITIES	32,681,893	28,416,031
COMMITMENTS & CONTINGENCIES		
STOCKHOLDERS EQUITY:		
Preferred stock, no par value, 8,000,000 shares authorized, none issued and outstanding		
Common stock, $.10 par value, 100,000,000 shares authorized, 13,091,088 shares issued and outstanding at March 31, 2008 and September 30, 2007, respectively	1,309,110	1,309,110
Additional paid-in capital	52,581,524	52,378,437
Retained earnings	1,403,998	4,585,007
Accumulated other comprehensive gain cumulative translation adjustment	32,213	88,670
Total Stockholders Equity	55,326,845	58,361,224

TOTAL LIABILITIES AND STOCKHOLDERS EQUITY	$ 88,008,738	$ 86,777,255

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements.

Table of Contents

SUNAIR SERVICES CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
FOR THE SIX MONTHS ENDED MARCH 31, 2008 AND 2007
(UNAUDITED)

	2008	2007
SALES		
Lawn and pest control services sales	$ 27,647,194	$ 25,990,136
Telephone communications sales	5,049,233	5,875,549
Total sales	32,696,427	31,865,685
COST OF SALES		
Lawn and pest control services cost of sales	10,425,089	9,319,837
Telephone communications cost of sales	2,338,867	3,219,253
Total cost of sales	12,763,956	12,539,090
GROSS PROFIT	19,932,471	19,326,595
SELLING, GENERAL AND ADMINISTRATIVE EXPENSES	22,462,331	19,982,156
LOSS FROM OPERATIONS	(2,529,860)	(655,561)
OTHER INCOME (EXPENSES):		
Interest income	122,331	119,418
Interest expense	(728,140)	(675,713)
(Loss) gain on disposal of assets	(6,157)	10,518
Total Other Income (Expenses)	(611,966)	(545,777)
LOSS FROM OPERATIONS BEFORE INCOME TAXES	(3,141,826)	(1,201,338)
INCOME TAX (PROVISION) BENEFIT	(39,183)	269,991
LOSS FROM CONTINUING OPERATIONS	(3,181,009)	(931,347)
INCOME FROM DISCONTINUED OPERATIONS, NET OF INCOME TAX PROVISION OF $0 and $562,933 IN 2008 and 2007, RESPECTIVELY		1,312,060
NET (LOSS) INCOME	$ (3,181,009)	$ 380,713

BASIC AND DILUTED (LOSS) INCOME PER SHARE:		
CONTINUING OPERATIONS	$ (0.24)	$ (0.07)
DISCONTINUED OPERATIONS	$	$ 0.10
NET (LOSS) INCOME	$ (0.24)	$ 0.03
WEIGHTED AVERAGE SHARES OUTSTANDING:		
BASIC and DILUTED	13,091,088	13,041,634

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements.

Table of Contents

SUNAIR SERVICES CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
FOR THE THREE MONTHS ENDED MARCH 31, 2008 AND 2007
(UNAUDITED)

	2008	2007
SALES		
Lawn and pest control services sales	$ 14,198,297	$ 13,601,619
Telephone communications sales	2,578,029	3,316,464
Total sales	16,776,326	16,918,083
COST OF SALES		
Lawn and pest control services cost of sales	5,458,133	4,758,071
Telephone communications cost of sales	1,186,723	1,732,989
Total cost of sales	6,644,856	6,491,060
GROSS PROFIT	10,131,470	10,427,023
SELLING, GENERAL AND ADMINISTRATIVE EXPENSES	10,868,570	10,345,084
(LOSS) INCOME FROM OPERATIONS	(737,100)	81,939
OTHER INCOME (EXPENSES):		
Interest income	68,427	51,644
Interest expense	(348,513)	(387,390)
(Loss) gain on disposal of assets	(10,827)	32,224
Total Other Income (Expenses)	(290,913)	(303,522)
LOSS FROM OPERATIONS BEFORE INCOME TAXES	(1,028,013)	(221,583)
INCOME TAX (PROVISION)	(39,183)	(47,312)
(LOSS) FROM CONTINUING OPERATIONS	(1,067,196)	(268,895)
INCOME FROM DISCONTINUED OPERATIONS, NET OF INCOME TAX BENEFIT OF $0 and $206,770 IN 2008 and 2007, RESPECTIVELY		49,917
NET (LOSS)	$ (1,067,196)	$ (218,978)

BASIC AND DILUTED (LOSS) PER SHARE:		
CONTINUING OPERATIONS	$ (0.08)	$ (0.02)
DISCONTINUED OPERATIONS	$	$ 0.00
NET (LOSS) INCOME	$ (0.08)	$ (0.02)
WEIGHTED AVERAGE SHARES OUTSTANDING:		
BASIC and DILUTED	13,091,088	13,066,578

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements.

Table of Contents

SUNAIR SERVICES CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS EQUITY AND COMPREHENSIVE (LOSS) INCOME
FOR THE SIX MONTHS ENDED MARCH 31, 2008
(UNAUDITED)

	Common Stock		Additional Paid-in	Retained	Accumulated Other Comprehensive Income	Total Stockholders
	Shares	Amount	Capital	Earnings	(Loss)	Equity
Balance at September 30, 2007	13,091,088	$ 1,309,110	$ 52,378,437	$ 4,585,007	$ 88,670	$ 58,361,224
Comprehensive income:						
Net (loss)				(3,181,009)		(3,181,009)
Currency translation adjustment					(56,457)	(56,457)
Comprehensive (loss)				(3,181,009)	(56,457)	(3,237,466)
Share-based compensation			203,087			203,087
Balance at March 31, 2008	13,091,088	$ 1,309,110	$ 52,581,524	$ 1,403,998	$ 32,213	$ 55,326,845

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements.

Table of Contents

SUNAIR SERVICES CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
FOR THE SIX MONTHS ENDED MARCH 31, 2008 AND 2007
(UNAUDITED)

	2008	2007
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net (loss) income	$ (3,181,009)	$ 380,713
Adjustments to reconcile net (loss) income to net cash (used in) provided by operating activities:		
Depreciation	454,946	470,443
Amortization	1,952,805	1,159,023
Deferred taxes		269,100
Bad debt reserve		5,747
Inventory reserve	(423,193)	77,962
Loss (gain) on sale of assets	6,157	(2,380,398)
Stock-based compensation expense	203,087	240,808
Stock issued for services rendered		45,000
(Increase) decrease in assets:		
Accounts receivable	(1,214,763)	(1,644,822)
Income tax receivable		23,842
Inventories	202,980	(351,078)
Prepaid and other current assets	400,471	(411,620)
Other assets	3,875	393,372
Increase (decrease) in liabilities:		
Accounts payable and accrued expenses	(758,450)	2,327,681
Unearned revenue	50,619	67,321
Income taxes payable		(1,057)
Customer deposits	392,892	134,091
Net Cash (Used In) Provided By Operating Activities	(1,909,583)	806,128
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchase of property, plant, and equipment	(289,352)	(202,470)
Software development costs		(162,018)
Cash paid for business acquisitions	(1,000,000)	(1,518,432)
Net proceeds from sale of assets	30,796	2,531,963
Net Cash (Used In) Provided by Investing Activities	(1,258,556)	649,043

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements.

Table of Contents

SUNAIR SERVICES CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
FOR THE SIX MONTHS ENDED MARCH 31, 2008 AND 2007
(UNAUDITED)

	2008	2007
CASH FLOWS FROM FINANCING ACTIVITIES:		
Repayment of line of credit (net)		(900,000)
Proceeds from line of credit	3,800,000	
Repayment of notes payable and capital leases	(80,638)	(56,707)
Net Cash Provided By (Used In) Financing Activities	3,719,362	(956,707)
Effect of exchange rate fluctuations on cash	(56,457)	99,867
NET INCREASE IN CASH AND CASH EQUIVALENTS	494,766	598,331
CASH AND CASH EQUIVALENTS, BEGINNING OF PERIOD	2,781,838	1,601,110
CASH AND CASH EQUIVALENTS, END OF PERIOD	$ 3,276,604	$ 2,199,441
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:		
Cash paid during the period for income taxes	$	$
Cash paid during the period for interest	$ 676,228	$ 549,113
SUPPLEMENTAL DISCLOSURE OF NON-CASH INVESTING AND FINANCING ACTIVITIES:		
Common stock issued in acquisition	$	$ 300,000
Debt incurred in acquisitions	$ 600,000	$ 1,500,000

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements.

Table of Contents

SUNAIR SERVICES CORPORATION AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

1. Basis of Consolidated Financial Statement Presentation

The accompanying unaudited condensed consolidated financial statements include the accounts of Sunair Services Corporation and its subsidiaries (the Company), required to be consolidated in accordance with U.S. generally accepted accounting principles (GAAP). The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with the accounting policies described in the September 30, 2007 Annual Report on Form 10-K except for the accounting policy relating to accounting for uncertainty in income taxes, and should be read in conjunction with the consolidated financial statements and notes thereto.

The unaudited condensed consolidated financial statements for the six and three months ended March 31, 2008 and 2007 included herein have been prepared in accordance with the instructions for Form 10-Q under the Securities Exchange Act of 1934, as amended, and Article 8 of Regulation S-X under the Securities Act of 1933, as amended. Certain information and footnote disclosures normally included in financial statements prepared in conformity with accounting principles generally accepted in the United States of America have been condensed or omitted pursuant to such rules and regulations relating to interim financial statements.

In the opinion of management, the accompanying unaudited condensed consolidated financial statements contain only normal recurring adjustments necessary to present fairly the Company s financial position as of March 31, 2008, and the results of its operations and cash flows for the six and three months ended March 31, 2008 and 2007. Operating results for the six months ended March 31, 2008 are not necessarily indicative of the results that may be expected for the fiscal year ending September 30, 2008.

2. Summary of Significant Accounting Policies

Income taxes

Effective October 1, 2007, the Company adopted Financial Accounting Standards Board (FASB) Interpretation No. (FIN) 48, Accounting for Uncertainty in Income Taxes. FIN 48 clarifies the accounting for uncertainty in income taxes recognized in financial statements in accordance with SFAS No. 109, Accounting for Income Taxes. FIN 48 prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. FIN 48 requires that the Company determine whether the benefits of the Company s tax positions are more likely than not of being sustained upon audit based on the technical merits of the tax position. The provisions of FIN 48 also provide guidance on de-recognition, classification, interest and penalties, accounting in interim periods, and disclosure. The Company did not have any unrecognized tax benefits and there was no effect on the financial condition or results of operations as a result of implementing FIN 48. The Company does not have any interest and penalties in the statement of operations for the six and three months ended March 31, 2008. The tax years 2004-2007 remain subject to examination by major tax jurisdictions.

Reclassification

Certain reclassifications of amounts previously reported have been made to the accompanying consolidated financial statements in order to maintain consistency and comparability between periods presented.

In August 2007, the Company sold all the issued and outstanding common stock of Percipia, Inc. (Percipia). For purposes of comparability, the results of these operations have been reclassified from continuing operations to discontinued operations for the six months ended March 31, 2007 presented in the accompanying condensed consolidated statements of operations. See Note 10- Discontinued Operations.

Recent Accounting Pronouncements

In December 2007, the FASB issued SFAS No. 141 (revised 2007) *Business Combinations* (FASB No. 141(R)). FASB No. 141(R) retains the fundamental requirements of the original pronouncement requiring that the purchase method be used for all business combinations. FASB No. 141(R) defines the acquirer as the entity that obtains control of one or more businesses in the business combination, establishes the acquisition date as the date that the acquirer achieves control and requires the acquirer to recognize the assets acquired, liabilities assumed and any non-controlling interest at their fair values as of the acquisition date. FASB No. 141(R) also requires that acquisition-related costs be recognized separately from the acquisition. FASB No. 141(R) is effective for the Company for fiscal 2010. The

Company is currently assessing the impact of FASB No. 141(R) on its consolidated financial position and results of operations.

Table of Contents

In December 2007, the FASB issued Statement No. 160, *Noncontrolling Interests in Consolidated Financial Statements an amendment of ARB No. 51 (FASB No. 160)* . The objective of FASB No. 160 is to improve the relevance, comparability, and transparency of the financial information that a reporting entity provides in its consolidated financial statements by establishing accounting and reporting standards for the noncontrolling interest in a subsidiary and for the deconsolidation of a subsidiary. This Statement applies to all entities that prepare consolidated financial statements, except not-for-profit organizations. FASB No. 160 amends ARB 51 to establish accounting and reporting standards for the noncontrolling interest in a subsidiary and for the deconsolidation of a subsidiary. It also amends certain of ARB 51 s consolidation procedures for consistency with the requirements of FASB No. 141 (R). This Statement is effective for fiscal years, and interim periods within those fiscal years, beginning on or after December 15, 2008 (that is, January 1, 2009, for entities with calendar year-ends). Earlier adoption is prohibited. The effective date of this Statement is the same as that of the related Statement 141(R). FASB No. 160 will be effective for the Company s fiscal year 2010. This Statement shall be applied prospectively as of the beginning of the fiscal year in which this Statement is initially applied, except for the presentation and disclosure requirements. The presentation and disclosure requirements shall be applied retrospectively for all periods presented. The Company is currently assessing the impact of FASB No. 160 on its consolidated financial statements.

In February 2007, the FASB issued Statement No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities including an amendment of FASB Statement No. 115* (FASB No. 159). FASB No. 159 gives the Company the irrevocable option to carry most financial assets and liabilities at fair value, with changes in fair value recognized in earnings. FASB No. 159 is effective for the Company s 2009 fiscal year, although early adoption is permitted. The Company is currently assessing the impact of FASB No. 159 on its consolidated financial statements.

In September 2006, the FASB issued Statement No. 157, *Fair Value Measurements* (FASB No. 157). FASB No. 157 provides a common definition of fair value and establishes a framework to make the measurement of fair value in generally accepted accounting principles more consistent and comparable. FASB No. 157 also requires expanded disclosures to provide information about the extent to which fair value is used to measure assets and liabilities, the methods and assumptions used to measure fair value, and the effect of fair value measures on earnings. On December 14, 2007, the FASB issued proposed FASB Staff Position No. FAS 157-b, Effective Date of FASB No. 157 (Proposed FSP). The Proposed FSP would amend FASB No. 157, to delay the effective date of FASB No. 157 for all nonfinanical assets and nonfinancial liabilities, except those that are recognized or disclosed at fair value in the financial statements on a recurring basis (that is, at least annually). The Proposed FSP defers the effective date of FASB No. 157 to fiscal years beginning after November 15, 2008, and interim periods within those fiscal years for items within the scope of the Proposed FSP. FASB No. 157 will be effective for the Company s 2010 fiscal year, although early adoption is permitted. The Company is currently assessing the potential effect of FASB No. 157 on its consolidated financial statements.

3. Acquisitions

Acquisition of Marshall Pest Control of SW FL, Inc.

On October 2, 2007, Middleton Pest Control, Inc. (Middleton) acquired substantially all the assets of Marshall Pest Control of SW FL, Inc. (Marshall) , a lawn and pest control services company located in Naples, Florida for $1.6 million, consisting of $1.0 million in cash and $600,000 in the form of a promissory note. In addition, the Company incurred working capital adjustments and transaction costs of approximately $0.3 million.

The following table sets forth the allocation of the purchase price to Marshall tangible and intangible assets acquired and liabilities assumed as of October 2, 2007:

Goodwill	$ 1,487,775
Customer list	225,204
Accounts receivable	68,989
Inventory	13,199
Fixed assets	62,475
Total	$ 1,857,642

11

Table of Contents

Acquisition of Archer Exterminators, Inc. (Archer)

On November 30, 2006, Middleton entered into an Asset Purchase Agreement to acquire substantially all of the assets of Archer for $3,300,000 consisting of $1,500,000 cash, $1,500,000 in the form of a subordinated promissory note and 73,529 shares of the Company s common stock valued at $300,000. In addition, the Company incurred working capital adjustments and transaction costs totaling $0.1 million. The shares were issued in January, 2007.

Acquisition of Valentine s Indoor Pest Management, Inc. (Valentine)

On February 8, 2007, Middleton acquired substantially all the assets of Valentine, headquartered in St. Cloud, Florida for approximately $43,400, consisting of $18,432 in cash and $25,000 in the form of a promissory note.

Acquisition of David Burke, Inc. D/B/A Florida Exterminating (Florida Exterminating)

On April 30, 2007, Middleton acquired substantially all the assets of Florida Exterminating, a pest control company headquartered in Tampa, Florida for approximately $815,000 consisting of $580,000 in cash and $235,000 in the form of a promissory note.

Acquisition of Summer Rain Fertilization Company (Summer Rain)

On May 31, 2007, Middleton acquired substantially all the assets of Summer Rain, a lawn care services company headquartered in Margate, Florida for approximately $1.0 million, consisting of $500,000 in cash and $500,000 in the form of a promissory note.

Acquisition of Howell Environmental, Inc. (Howell)

On August 21, 2007, Middleton acquired substantially all the assets of Howell, a lawn care and pest control services company located in West Palm Beach, Florida, for approximately $2.3 million, consisting of $925,000 in cash and $1.4 million in the form of a promissory note with $1.0 million secured by a letter of credit.

Acquisition of Longboat Key Pest Control, Inc. (Longboat Key)

On September 20, 2007, Middleton acquired substantially all of the assets of Longboat Key, a lawn care and pest control services company located in Longboat, Florida for $1.7 million, consisting of $1.0 million in cash, $542,000 in the form of a promissory note and $158,000 to be paid over a two year period at 50% of the cash collections related to a large commercial customer. The $158,000 is considered contingent purchase price and will be recorded as part of the purchase price at the time it becomes probable that the contingency will be resolved and payment will be received.

Purchase Price Allocation

The following table sets forth the allocation of the purchase price for tangible and intangible assets associated with the above 2007 and 2008 acquisitions and their related acquired assets and liabilities assumed as of March 31, 2008:

Goodwill	$ 9,344,859
Customer list	2,159,885
Accounts receivable	641,666
Inventory	62,418
Fixed assets	576,424
Prepaid expenses	210,644
Customer deposits	(79,281)
Deferred revenue	(677,539)
Total	$ 12,239,076

Table of Contents

Pro-Forma Results of Operations

The following sets forth the Company s results of operations for the six months ended March 31, 2007 as if the acquisitions had taken place on October 1, 2006.

	For the Three Months Ended March 31, 2007	For the Six Months Ended March 31, 2007
Revenues	$ 18,584,507	$ 35,590,962
Net income	$ 205,744	$ 1,146,631
Net income per share		
Basic and diluted	$ 0.02	$ 0.09

The pro-forma results of operations for the three and six months ended March 31, 2008 are not presented since there was an insignificant difference between pro-forma and actual results for the period as our sole acquisition Marshall was acquired on October 2, 2007.

4. Note Receivable

Pursuant to the Asset Purchase Agreement on September 8, 2006 between the Company and Sunair Electronics, LLC formerly known as Sunair Holdings, LLC (Sunair Holdings), the Company received a three year subordinated promissory note as partial payment for the sale of substantially all of the assets of Sunair Communications, Inc. (Sunair Communications). The $2.0 million note issued by Sunair Holdings is guaranteed by the members of Sunair Holdings, matures on September 8, 2009 and bears interest at one year London Interbank Offering Rate (LIBOR) plus 3% (5.49% at March 31, 2008) which is payable monthly starting on October 1, 2006. Accrued interest income through March 31, 2008, included in prepaid and other current assets in the accompanying condensed consolidated balance sheets amounted to $57,132. At September 30, 2007 accrued interest income amounted to $55,560. The Company s former Chief Financial Officer, who also was the former Chief Financial Officer of Sunair Communications, and the Company s former President, who also was the former President of Sunair Communications, are also affiliates of Sunair Holdings.

Table of Contents

5. Revolving Line of Credit

The Company has a line of credit with a financial institution collateralized by substantially all of the assets of the Company. The maximum credit limit was $13.5 million as of March 31, 2008. Interest is compounded daily based upon the LIBOR plus 5.0%. The interest rate at March 31, 2008 was approximately 7.49%. The revolving line of credit has a commitment fee in the amount of .375% per annum on the average daily unused amount of the aggregate revolving committed amount. The outstanding balance on the revolving line of credit at March 31, 2008 and September 30, 2007, respectively, amounted to $10,532,796 and $6,732,796. At March 31, 2008, the availability under the revolving line of credit amounted to $1,967,204 which is net of a $1.0 million outstanding letter of credit.

On May 14, 2007, the Company amended the terms of its credit agreement to extend the maturity date to April 1, 2008 and to reduce the capacity under the revolving line of credit from $20.0 million to $16.0 million. This amendment also modified certain financial covenants. The leverage ratio was increased and the consolidated EBITDA requirement was reduced. On August 14, 2007, the Company obtained a subsequent extension of the maturity date on the credit agreement to October 1, 2008.

On February 12, 2008, the Company amended certain terms and conditions of the credit agreement. Among the amended terms and conditions were an extension of the maturity date to January 7, 2009 as well as amendments to the financial covenants relating to consolidated EBITDA, the leverage ratio and the fixed charge coverage ratio, which amendments are effective as of December 31, 2007. As of March 31, 2008, the Company was in compliance with its financial covenants.

6. Notes Payable

The Company has a capital lease for certain office equipment. The balance of the capital lease at March 31, 2008 and September 30, 2007, totaled $14,643 and $16,353, respectively.

The Company has notes payable with a financial institution for leased office build out costs and computer equipment. The notes bear interest at 5.60% and 5.25% per annum, respectively, payable in monthly installments of principal and interest in the amount of $3,285 through March 29, 2011 and $5,795 through September 20, 2008, respectively. Balances at March 31, 2008 and September 30, 2007, totaled $142,666 and $192,367, respectively.

The Company has notes payable with financial institutions for automobile loans. Interest rates range from 0% to 9% per annum, payable in monthly installments of principal and interest ranging in the amounts of $220 to $687, expiring in various years through 2010. Balances at March 31, 2008 and September 30, 2007, totaled $39,538 and $68,765, respectively.

Table of Contents

The Company has notes payable relating to certain acquisitions as described in Note 3- Acquisitions which bear interest at 6% and 7%, with one note payable bearing interest at LIBOR plus 2% per annum (4.49% at March 31, 2008), with interest payable in semi-annual installments ranging in the amounts of $3,000 to $49,000 and principal due at maturity. The notes expire in various years through 2011. The note payable balances for the acquisition debt at March 31, 2008 and September 30, 2007, totaled $6,277,000 and $5,677,000, respectively.

Interest expense incurred for the notes payable amounted to $217,528 and $107,640 for the six and three months ended March 31, 2008, respectively, and $91,557 and $54,643 for the six and three months ended March 31, 2007, respectively.

Minimum future principal payments required under the above notes payable as of March 31, 2008, for each of the next five years and in the aggregate are:

2008	$ 1,838,327
2009	2,056,599
2010	1,435,104
2011	1,143,817
2012	
Thereafter	
	6,473,847
Less: current portion	1,838,327
Long term portion	$ 4,635,520

7. Notes Payable-Related Party

The Company has a $5,000,000 subordinated note payable to related parties, in connection with the acquisition of Middleton. As of March 31, 2008 these related parties include Charles Steinmetz, the former CEO of Middleton from 1977 through June 2005 and the current CEO, who was appointed to serve as CEO of Middleton again effective January 18, 2008. Mr. Steinmetz was the majority owner of Middleton from 1977 until it was purchased by the Company in June 2005 and has served as a director of the Company since that time. Interest is paid semi-annually at prime (5.25% as of March 31, 2008). The note payable is due in full on June 7, 2010. Interest expense related to this note payable amounted to $183,835 and $75,068, for the six and three months ended March 31, 2008, respectively, and $207,250 and $102,966 for the six and three months ended March 31, 2007, respectively.

8. Income Taxes

The Company did not have an income tax provision or benefit for the six and three months ended March 31, 2008, respectively, as the Company has $13.5 million of net operating losses carryforwards which expire in 2026 and which are fully reserved. In addition, the Company does not have any net operating loss carrybacks. As a result the Company was unable to recognize an income tax benefit for the three and six months ended March 31, 2008. The income tax provision of $39,183 for the three months ended March 31, 2008 relates to foreign income taxes incurred by Telecom FM. For the six and three months ended March 31, 2007, the Company had an income tax benefit (provision) of $269,991 and ($47,312) for continuing operations, respectively.

9. Stock Options

At the annual meeting of shareholders held on February 4, 2005, the shareholders approved the adoption of the Company s 2004 Stock Incentive Plan with an aggregate of 800,000 shares of the Company s unissued common stock, to replace the Company s 2000 Stock Option Plan, which was approved by the Company s shareholders at a shareholders meeting held on January 24, 2000. The 800,000 shares authorized under the 2004 Stock Incentive Plan are reserved for issuance to officers, directors, employees and prospective employees as incentive stock options, non-qualified stock options, restricted stock awards, other equity awards and performance based stock incentives. The option price, numbers of shares and grant date are determined at the discretion of the Company s board of directors or the committee overseeing the 2004 Stock Incentive Plan.

There were 369,000 and 35,000 options granted during the three months ended March 31, 2008 and 2007, respectively.

Table of Contents

Stock options activity for the six months ended March 31, 2008 is as follows:

	Shares	Weighted Avg. Exercise Price	Remaining Life
Balances, beginning of period	585,092	$ 6.94	
Granted	369,000	$ 1.76	
Exercised		$	
Expired/Forfeited	(58,476)	$ 8.15	
Options outstanding, end of period	895,616	$ 4.55	6.30
Options exercisable, end of period	443,685	$ 6.44	5.09
Options available for future grants	111,051		

Included in the 895,616 options outstanding are 206,667 options that were granted outside of the 2004 Stock Incentive Plan.

Fair Value

On January 1, 2006, the Company adopted the provisions of FASB No. 123R which requires the Company to recognize expense related to the fair value of stock-based compensation awards. The Company elected the modified prospective transition method as permitted by FASB No. 123R, under which stock-based compensation for the six and three months ended March 31, 2008 and 2007 is based on grant date fair value estimated in accordance with the provisions of FASB No. 123R and compensation expense for all stock-based compensation awards granted subsequent to January 1, 2006, as well as the unvested portion of previously granted awards that remained outstanding as of January 1, 2006 based on the grant date fair value estimated in accordance with the provisions of FASB No. 123R. In addition, options granted to certain members of the board of directors as payment for Board services recorded in accordance with FASB No. 123R and the issuance of restricted stock awards and stock units are also included in stock-based compensation for the six and three months ended March 31, 2008 and 2007. The Company recognizes compensation expense for restricted stock awards and restricted stock units on a straight-line basis over the requisite service period of the award. The Company recorded $203,087 and $61,075 of stock-based compensation expense which has been classified as selling, general and administrative expenses for the six and three months ended March 31, 2008, respectively, and $240,808 and $23,824 for the six and three months ended March 31, 2007, respectively.

The fair value of stock-based awards was estimated using the Black-Scholes model, on the date of grant, with the following weighted-average assumptions:

	For the Six Months Ended March 31,	
	2008	2007
Expected dividend yield		
Expected price volatility	63.76-64.36%	65.21-70.07%
Risk-free interest rate	2.8-3.09%	3.76-4.61%
Expected life of options	4.50-5.25 years	5-8.25 years

The Company s computation of the expected volatility for the six months ended March 31, 2008 and 2007 is based primarily upon historical volatility and the expected term of the option. The Company continues to use the simplified method of determining the expected term provided under SAB 110 as sufficient historical data is not available. The interest rate is based on the U.S. Treasury yield in effect at the time of grant for a period commensurate with the estimated expected life.

As of March 31, 2008, approximately $811,657 of total unrecognized compensation costs related to non-vested stock options is expected to be recognized over a weighted average period of 2.51 years.

16

Table of Contents

10. Discontinued Operations

On August 1, 2007, the Company sold all the outstanding shares of Percipia, a wholly-owned subsidiary, in our Telephone Communications segment for approximately $4.0 million in cash, of which $750,000 was placed in an escrow account pending the resolution of certain tax matters.

On November 20, 2006, the Company closed a transaction to sell the real estate property associated with the previously sold high frequency radio business for $2.7 million in cash and a recognized gain in the amount of $2.2 million, $1.4 million net of income taxes.

The accompanying consolidated condensed statements of operations for the six months presented have been adjusted to classify Percipia as discontinued operations. Selected statements of operations data for the Company s discontinued operations is as follows:

	(dollars in thousands) For the Six Months Ended March 31, 2007
Percipia, Inc. Net loss	$ (308)
Pre-tax (loss) from discontinued operations	(308)
Income tax benefit	259
(Loss) from discontinued operations, net of income taxes	(49)
Gain on sale of assets from discontinued operations	2,183
Income tax (provision)	(822)
Gain on sale of assets from discontinued operations, net of income taxes	1,361
Income from discontinued operations, net of income taxes	$ 1,312

11. Commitments and Contingencies

The Company leases office space under operating leases expiring in various years through 2012, and vehicles under operating leases expiring in various years through 2014. Certain leases provide for renewal options for periods from one to five years at their fair rental value at the time of renewal. In the normal course of business, operating leases are generally renewed or replaced by other leases. Rent expense and vehicle lease expense was $1,792,213 and $954,846 for the six and three months ended March 31, 2008, respectively, and $1,653,070 and $834,554 for the six and three months ended March 31, 2007, respectively.

Litigation

We are involved in litigation from time to time in the ordinary course of our business. Except for the litigation described below, we do not believe that any litigation in which we are currently involved, individually or in the aggregate, is material to our financial condition or results of operations.

In October 2007, the Company filed a lawsuit in the Circuit Court for the Ninth Judicial Circuit in the State of Florida against a number of former employees of Middleton for violation of their non-compete agreements. In addition, certain of these former employees pursued and hired away employees of Middleton which is also a violation of the existing employee non-compete agreements. The Company is seeking injunctive relief and damages. In October 2007, the Company also filed a lawsuit against a competitor for tortious interference as they hired these former employees knowing that they were in violation of the Company s non-compete agreement. This matter was settled during the three months ended March 31, 2008 for an immaterial amount.

Table of Contents

12. Goodwill and Intangible Assets

Goodwill and intangible assets consist of the following at March 31, 2008 and September 30, 2007:

	Goodwill	Customer Lists	Total
Ending balance, September 30, 2007	$ 60,675,353	$ 10,958,234	$ 71,633,587
Acquisition of businesses	1,487,775	225,204	1,712,979
Purchase price adjustment	(50,600)		(50,600)
	62,112,528	11,183,438	73,295,966
Less amortization expense		(1,864,533)	(1,864,533)
Ending balance, March 31, 2008	$ 62,112,528	$ 9,318,905	$ 71,431,433

The table below presents the weighted average life in years of the Company s intangible assets.

	2008	2007
Goodwill	(a)	(a)
Customer lists (b)	5	8
Weighted average	5	8

(a) Goodwill is not amortized but, along with all other intangible assets, is reviewed for possible impairment each year at September 30th or when indicators of impairment exist.

(b) Change in estimated useful life for customer lists during the fourth quarter of 2007.

The table below reflects the estimated aggregate customer account amortization for each of the five succeeding years of the Company s existing customer account base as of March 31, 2008:

	Aggregate Amortization Expense
2008	$ 3,724,403
2009	3,724,403
2010	1,426,743
2011	384,060
2012	59,296
Total Aggregate Amortization Expense	$ 9,318,905

13. Net Income (Loss) Per Share

Basic net income (loss) per share is computed using the weighted average number of shares outstanding during the period. Due to the Company s losses from continuing operations, dilutive potential common shares in the form of warrants were excluded from the computation of diluted loss per share, as inclusion would be anti-dilutive for the periods presented.

Table of Contents

14. Segment and Geographic Information

The Company manages its business and has segregated its activities into two business segments; (i) Pest control, lawn and shrub care, subterranean and drywood termite control and mosquito reduction services and (ii) installation and maintenance of telephone communication systems.

Certain financial information for each segment is provided below as of March 31, 2008 and September 30, 2007, and for the six months ended March 31, 2008 and 2007:

	For the Six Months Ended March 31,	
	2008	**2007**
Net revenues:		
Lawn and pest control services	$ 27,647,194	$ 25,990,136
Telephone communications	5,049,233	5,875,549
Total net revenues	$ 32,696,427	$ 31,865,685
Operating income (loss):		
Lawn and pest control services	$ 1,523,281	$ 2,555,710
Telephone communications	332,231	228,404
Unallocated home office expenses	(4,385,372)	(3,439,675)
Total operating loss	$ (2,529,860)	$ (655,561)

	March 31, 2008	**September 30, 2007**
Identifiable property plant and equipment:		
Lawn and pest control services	$ 1,988,340	$ 2,062,451
Telephone communications	40,741	56,101
Total identifiable property plant and equipment	$ 2,029,081	$ 2,118,552

The Company operates worldwide, primarily in North America. Middleton operates entirely within the State of Florida and Telecom FM operates primarily in Spain, the United Kingdom and Italy.

15. Related Parties

The Company pays management fees to RPC Financial Advisors, LLC (RPC), a related party. On January 7, 2008, the Company entered into a management services agreement (Management Services Agreement or the Amended Management Services Agreement) with RPC, which supersedes and replaces the management services agreement (the Previous Management Services Agreement) dated February 8, 2005, as amended, between the Company and RPC. Pursuant to the Amended Management Services Agreement, the Company provided RPC with notice that the Previous Management Services Agreement would not be renewed and that the Amended Management Services Agreement would be effective as of February 8, 2008.

The Amended Management Services Agreement is for a term of three years which commenced on February 8, 2008 and expires on February 7, 2011. The Company will pay RPC a monthly management fee equal to one (1%) of the monthly gross revenues of the Company, which will be payable monthly based on the average monthly revenues of the preceding quarter. RPC will also receive a transaction fee of up to 2% of the Aggregate Consideration received by the Company in a Transaction (as such capitalized terms are defined in the Management Services Agreement). Pursuant to the Management Services Agreement, RPC will provide the Company with services similar to those

provided in the Previous Management Services Agreement. After the initial term of three years, the Management Services Agreement will automatically renew for successive one year terms, unless either RPC or the Company terminates the agreement upon 30 days notice. Management fees for the six and three months ended March 31, 2008 totaled $689,470 and $298,845, respectively, and $782,394 and $390,625 for the six and three months ended March 31 2007, respectively.

Table of Contents

The Company issued a note payable to related parties in connection with the acquisition of Middleton, as discussed in Note 7-Note Payable-Related Party.

The Company received a note receivable from former related parties through the sale of Sunair Communications, the high frequency radio segment, as more fully described in Note 4-Note Receivable.

Item 2. ***Management s Discussion And Analysis of Financial Condition and Results of Operations***

Cautionary Statement Regarding Forward Looking Information:

Some of the statements in this quarterly report, including those that contain the words anticipate, believe, plan, estimate, expect, should, intend and other similar expressions, are forward-looking statements within the meanin the Private Securities Litigation Reform Act of 1995. Those forward-looking statements involve known and unknown risks, uncertainties and other factors that may cause our actual results, performance or achievements or those of our industry to be materially different from any future results, performance or achievements expressed or implied by those forward-looking statements. Among the factors that could cause actual results, performance or achievement to differ materially from those described or implied in the forward-looking statements are general economic conditions, competition, potential technology changes, changes in or the lack of anticipated changes in the regulatory environment in various countries, the risks inherent in new product and service introductions and the entry into new geographic markets and other factors included in our Annual Report on Form 10-K for the fiscal year ended September 30, 2007 filed with the Securities and Exchange Commission (the SEC) on January 15, 2008 and other filings with the SEC. Copies of our SEC filings are available from the SEC or may be obtained upon request from us. We do not undertake any obligation to update the information contained herein, which speaks only as of this date.

Company Overview

Sunair Services Corporation (the Company we or us) is a Florida corporation organized in 1956. We changed our corporate name from Sunair Electronics, Inc. to Sunair Services Corporation in November of 2005. Previously, we operated through two business segments: Telephone Communications and High Frequency Radio. In June 2005 with the acquisition of Middleton Pest Control, Inc. (Middleton) we embarked on a new strategy to become a leading regional provider of lawn and pest control services focusing mainly on residential customers.

In order to execute our strategy, we shifted our focus to the Lawn and Pest Control Services business segment, which resulted in a series of acquisitions and divestitures planned to enable us to shed our legacy businesses (Telephone Communications and High Frequency Radio) and grow our core business, lawn and pest control. We intend to divest ourselves of our remaining telecommunications subsidiary, Telecom FM Limited (Telecom FM), as soon as is practicable. However, we cannot assure you of the timing of such disposition, or the amount of net proceeds we will receive upon such disposition.

Table of Contents

To date the acquisitions and divestitures have been as follows:

Acquisitions:

June 2005 we acquired the issued and outstanding stock of Middleton, our platform company, a leading provider of lawn and pest control services in Florida.

July 2005 we acquired substantially all the assets of Four Seasons Lawn and Pest Control, Inc.

December 2005 we acquired substantially all the assets of Spa Creek Services, LLC, D/B/A as Pest Environmental Services, Inc.

January 2006 we acquired substantially all the assets of Par Pest Control, Inc., D/B/A Paragon Termite & Pest Control.

February 2006 we acquired substantially all the assets of Pestec Pest Control, Inc.

March 2006 we acquired substantially all the assets of Ron Fee, Inc.

November 2006 we acquired substantially all the assets of Archer Exterminators, Inc.

February 2007 we acquired substantially all the assets of Valentine s Indoor Pest Management, Inc.

April 2007 we acquired substantially all the assets of David Burke, Inc., D/B/A Florida Exterminating.

May 2007 we acquired substantially all the assets of Summer Rain Fertilization Company.

August 2007 we acquired substantially all the assets of Howell Environmental, Inc.

September 2007 we acquired substantially all the assets of Longboat Key Pest Control, Inc.

October 2007 we acquired substantially all the assets of Marshall Pest Control of SW FL, Inc.

All of these acquisitions of lawn care and pest control companies have been made by Middleton, our platform company, and are being integrated into its operations.

Dispositions:

September 2006 we sold substantially all the assets of Sunair Communications Inc., our high frequency radio business.

November 2006 we sold real estate associated with the previously sold high frequency radio business.

August 2007 we sold all the issued and outstanding stock of Percipia, Inc. (Percipia), a wholly-owned subsidiary in our telephone communications segment.

Table of Contents

Results of Operations

Results of Operations for the Three Months Ended March 31, 2008 as Compared to the Three Months Ended March 31, 2007.

Revenue:

	(dollars in thousands) For the Three Months Ended March 31,	
	2008	**2007**
Lawn and pest control services	$ 14,198	$ 13,602
Telephone communications	2,578	3,316
Total revenue	$ 16,776	$ 16,918

Lawn and Pest Control Services

Revenue from the lawn and pest control services segment is comprised of lawn, pest control and termite services. Revenue in the segment increased by $0.6 million or 4.4% for the three months ended March 31, 2008 as compared to the three months ended March 31, 2007. The revenue increase was primarily attributable to the integration of our acquisitions since December 31, 2006.

Telephone Communications

Our remaining telephone communications subsidiary, Telecom FM, manufactures and sells least-cost routing devices. Revenue from Telecom FM decreased by $0.7 million or 22.3% for the three months ended March 31, 2008 as compared to the three months ended March 31, 2007. During the second quarter of fiscal year 2007 Telecom FM received a series of large orders due to a change in legislation. This did not occur in the quarter ended March 31, 2008.

Cost of Sales:

	(dollars in thousands) For the Three Months Ended March 31,	
	2008	**2007**
Lawn and pest control services	$ 5,458	$ 4,758
Telephone communications	1,187	1,733
Total cost of sales	$ 6,645	$ 6,491

Lawn and Pest Control Services

Cost of sales in the lawn and pest control services segment increased by $0.7 million or 14.7% to $5.5 million or 38.4% of revenue for the three months ended March 31, 2008 as compared to $4.8 million or 35.0% of revenue for the three months ended March 31, 2007.

Chemical costs increased by $0.2 million for the three months ended March 31, 2008 as compared to the same period in 2007. The price of petro-based chemical and fertilizer products increased due to higher fuel prices.

Vehicle costs increased by $ 0.4 million for the three months ended March 31, 2008 compared to the same period in 2007 primarily due to an increase in fuel and vehicle maintenance costs.

Table of Contents

Telephone Communications

Cost of sales in our telephone communications segment decreased by $0.5 million or 31.5% to $1.2 million or 46.0% of revenue for the three months ended March 31, 2008 as compared to $1.7 million or 52.3% of revenue for the three months ended March 31, 2007, primarily related to a decrease in product costs due to a shift in product mix.

Gross Profit:

	(dollars in thousands) For the Three Months Ended March 31,	
	2008	**2007**
Lawn and pest control services	$ 8,740	$ 8,844
Telephone communications	1,391	1,583
Total gross profit	$ 10,131	$ 10,427

Lawn and Pest Control Services

The gross profit of the lawn and pest control services segment decreased by $0.1 million or 1.2% to $8.7 million or 61.6% of revenue for the three months ended March 31, 2008 as compared to $8.8 million or 65.0% of revenue for the three months ended March 31, 2007.

Telephone Communications

The gross profit in the telecommunications segment decreased by $0.2 million or 12.1% to $1.4 million for the three months ended March 31, 2007 as compared to $1.6 million for the three months ended March 31, 2007.

Gross profit decreased for the three months ended March 31, 2008 compared to the same time period in 2007 primarily due to a decrease in revenue. The gross margin increased to 54.0% in 2008 compared to 47.7% in 2007 due to a reduction in cost of sales resulting from a shift in product mix.

Operating Expenses:

Selling, General and Administrative Expenses:

	(dollars in thousands) For Three Months Ended March 31,	
	2008	**2007**
Selling	$ 1,918	$ 2,379
General and administrative	7,792	7,258
Depreciation and amortization	1,159	708
Total operating expenses	$ 10,869	$ 10,345

Table of Contents

Selling, general and administrative expenses (SG&A expense) increased by $0.5 million or 5.1% to $10.9 million or 64.8% of revenue for the three months ended March 31, 2008 as compared to $10.3 million or 61.1% of revenue for the three months ended March 31, 2007.

Selling expenses decreased by $0.5 million or 19.4% to $1.9 million or 11.4% of revenue for the three months ended March 31, 2008 as compared to $2.4 million or 14.1% of revenue for the three months ended March 31, 2007.

Middleton s selling costs decreased by $0.3 million for the three months ended March 31, 2008 as compared to the same time period in 2007 as a result of a decrease in advertising expense.

General and administrative expenses increased by $0.5 million or 7.4% to $7.8 million or 46.3% of revenue for the three months ended March 31, 2008 as compared to $7.4 million or 43.8% of revenue for the three months ended March 31, 2008.

Middleton s general and administrative expenses increased by $0.7 million for the three months ended March 31, 2008 as compared to the same period in 2007. The increase was primarily driven by payroll expenses which increased by $0.2 million for the three month period ended March 31, 2008 as compared to the same period in 2007 as a result of the purchase and integration of several acquisitions, expansion of staff related to meeting our compliance requirements with regards to Sarbanes-Oxley and an increase in staff related to the conversion of our existing operating software to a new system. Occupancy expenses increased by $0.1 million due to our expansion and increased facility lease rates. Health insurance expenses also increased by $0.1 million.

Depreciation and amortization expenses increased by $0.5 million or 63.9% to $1.2 million or 6.9 % of revenue for the three months ended March 31, 2008 as compared to $0.7 million or 4.2% of revenue for the three months ended March 31, 2007.

Corporate depreciation and amortization expenses increased by $0.5 million for the three months ended March 31, 2008 as compared to 2007 mostly attributable to an increase in the amortization of intangible assets due to our acquisition activity coupled with the change in estimated useful life for customer lists from 8 years to 5 years, which occurred during the fourth quarter of fiscal year 2007.

Other Income (Expenses):

	(dollars in thousands) For the Three Months Ended March 31,	
	2008	**2007**
Interest income	$ 69	$ 52
Interest expense	(349)	(388)
(Loss) gain on disposal of assets	(11)	32
Total other income (expenses)	$ (291)	$ (304)

Other expenses decreased by $13,000 or 4.3% for the three months ended March 31, 2008 as compared to the three months ended March 31, 2008.

Table of Contents

Income Tax (Provision) from Continuing Operations:

	(dollars in thousands) For the Three Months Ended March 31,	
	2008	**2007**
Income tax (provision)	$ (39)	$ (47)

The income tax provision from continuing operations decreased slightly for the three months ended March 31, 2008 as compared to the three months ended March 31, 2007. The income tax provision of $39,183 for the three months ended March 31, 2008 relates to foreign income taxes incurred by Telecom FM. The Company did not recognize an income tax benefit for the three months ended March 31, 2008 as the Company has $13.5 million of net operating losses carryforwards which expire in 2026 and which are fully reserved. In addition, the Company does not have any net operating loss carrybacks.

Discontinued Operations:

	(dollars in thousands) For the Three Months Ended March 31, 2007
Income from discontinued operations, net of income taxes	$ 50
Gain (loss) on sale of assets from discontinued operations, net of income taxes	
Income from discontinued operations, net of taxes	$ 50

As indicated earlier, our significant divestitures have been recorded as discontinued operations:

On August 1, 2007, we sold all the outstanding shares of Percipia. The results of operations for the three months ended March 31, 2007 related to Percipia have been classified as discontinued operations.

Table of Contents

Results of Operations

Results of Operations for the Six Months Ended March 31, 2008 as Compared to the Six Months Ended March 31, 2007.

Revenue:

	(dollars in thousands) For the Six Months Ended March 31,	
	2008	**2007**
Lawn and pest control services	$ 27,647	$ 25,990
Telephone communications	5,049	5,876
Total revenue	$ 32,696	$ 31,866

Lawn and Pest Control Services

Revenue from the lawn and pest control services segment is comprised of lawn, pest control and termite services. Revenue in the segment increased by $1.7 million or 6.4% for the six months ended March 31, 2008 as compared to the six months ended March 31, 2007. The revenue increase was primarily attributable to the integration of our acquisitions since December 31, 2006.

Telephone Communications

Our remaining telephone communications subsidiary, Telecom FM, manufactures and sells least-cost routing devices. Revenue from Telecom FM decreased by $0.8 million or 14.1% for the six months ended March 31, 2008 as compared to the six months ended March 31, 2007. During the second quarter of fiscal year 2007 Telecom FM received a series of large orders due to a change in legislation. This did not occur in the quarter ended March 31, 2008.

Cost of Sales:

	(dollars in thousands) For the Six Months Ended March 31,	
	2008	**2007**
Lawn and pest control services	$ 10,425	$ 9,320
Telephone communications	2,339	3,219
Total cost of sales	$ 12,764	$ 12,539

Lawn and Pest Control Services

Cost of sales in the lawn and pest control services segment increased by $1.1 million or 11.9% to $10.4 million or 37.7% of revenue for the six months ended March 31, 2008 as compared to $9.3 million or 35.9% of revenue for the six months ended March 31, 2007.

Chemical costs increased by $0.4 million for the six months ended March 31, 2008 as compared to the same period in 2007. The price of petro-based chemical and fertilizer products increased due to higher fuel prices.

Vehicle costs increased by $0.5 million for the six months ended March 31, 2008 compared to the same period in 2007 primarily due to an increase in fuel and vehicle maintenance costs.

Telephone Communications

Cost of sales in our telephone communications segment decreased by $0.9 million or 27.3% to $2.3 million or 46.3% of revenue for the six months ended March 31, 2008 as compared to $3.2 million or 54.8% of revenue for the six months ended March 31, 2007, primarily related to a decrease in product costs due to a shift in product mix.

Table of Contents

Gross Profit:

	(dollars in thousands) For the Six Months Ended March 31,	
	2008	**2007**
Lawn and pest control services	$ 17,222	$ 16,671
Telephone communications	2,710	2,656
Total gross profit	$ 19,932	$ 19,327

Lawn and Pest Control Services

The gross profit of the lawn and pest control services segment increased by $0.6 million or 3.3% to $17.2 million or 62.3% of revenue for the six months ended March 31, 2008 as compared to $16.7 million or 64.1% of revenue for the six months ended March 31, 2007.

The increase in gross profit of 3.3% for the six months ended March 31, 2008 over the same period in the prior year is proportionate to the increase in revenue during those periods.

Telephone Communications

The gross profit in the telecommunications segment increased by $0.1 million or 2.0% to $2.7 million for the six months ended March 31, 2007 as compared to $2.6 million for the six months ended March 31, 2007.

Gross profit increased for the six months ended March 31, 2008 compared to the same time period in 2007 despite a decrease in revenue. The gross margin increased to 53.7% in 2008 compared to 45.2% in 2007 due to a shift in product mix.

Operating Expenses:

Selling, General and Administrative Expenses:

	(dollars in thousands) For the Six Months Ended March 31,	
	2008	**2007**
Selling	$ 3,928	$ 4,209
General and administrative	16,204	14,394
Depreciation and amortization	2,330	1,379
Total operating expenses	$ 22,462	$ 19,982

Table of Contents

Selling, general and administrative expenses (SG&A expense) increased by $2.5 million or 12.4% to $22.5 million or 68.7% of revenue for the six months ended March 31, 2008 as compared to $20.0 million or 62.7% of revenue for the six months ended March 31, 2007.

Selling expenses decreased by $0.3 million or 6.7% to $3.9 million or 12.0% of revenue for the six months ended March 31, 2008 as compared to $4.2 million or 13.2% of revenue for the six months ended March 31, 2007.

Middleton s selling costs decreased by $0.2 million for the six months ended March 31, 2008 as compared to the same time period in 2007 as a result of reduction in advertising expense.

General and administrative expenses increased by $1.8 million or 12.6% to $16.2 million or 49.6% of revenue for the six months ended March 31, 2008 as compared to $14.4 million or 45.2% of revenue for the six months ended March 31, 2008.

Middleton s general and administrative expenses increased by $1.8 million for the six months ended March 31, 2008 as compared to the same period in 2007. The increase in general and administrative expenses was primarily driven by:

An increase in payroll expense of $0.7 million and an increase in payroll taxes of $0.1 million for the six month period ended March 31, 2008 as compared to the same period in 2007 as a result of the purchase and integration of several acquisitions, expansion of staff related to meeting our compliance requirements with regards to Sarbanes-Oxley and an increase in staff related to the conversion of our existing operating software to a new system.

Occupancy expenses increased by $0.2 million due to our expansion and increased facility lease rates.

The Company moved to a lockbox system in August 2007. Lockbox fees and statement fulfillment expenses were $0.2 million for the six months ended March 31, 2008. There were no lockbox fees and statement costs for the same time period in 2007. The implementation of a lockbox system has enabled us to streamline our cash receipts processing and has improved our cash flow.

Vehicle expenses increased by $0.2 million primarily due to higher fuel costs.

Professional fees increased by $0.3 million due to the temporary use of IT and marketing consultants.

Depreciation and amortization expenses increased by $0.9 million or 117.1% to $2.3 million or 7.1% of revenue for the six months ended March 31, 2008 as compared to $1.4 million or 4.3% of revenue for the six months ended March 31, 2007.

Corporate depreciation and amortization expenses increased by $1.0 million for the six months ended March 31, 2008 as compared to 2007 due to a significant increase in the amortization of intangible assets due to our acquisition activity coupled with the change in estimated useful life for customer lists from 8 years to 5 years, which occurred during the fourth quarter of fiscal year 2007.

Other Income (Expenses):

	(dollars in thousands) For the Six Months Ended March 31,	
	2008	**2007**
Interest income	$ 122	$ 119
Interest expense	(728)	(676)
(Loss) gain on disposal of assets	(6)	11
Total other income (expenses)	$ (612)	$ (546)

Other expenses increased by $0.1 million or 12.1% for the six months ended March 31, 2008 as compared to the six months ended March 31, 2008.

Middleton s interest expense increased by $0.1 million for the six months ended March 31, 2008 as compared to the six months ended March 31, 2007. The lawn and pest services segment incurred an additional $3.3 million in debt related to acquisitions since March 31, 2007.

Table of Contents

Income Tax (Provision) Benefit from Continuing Operations:

	(dollars in thousands) For the Six Months Ended March 31,	
	2008	**2007**
Income tax (provision) benefit	$ (39)	$ 270

Income tax benefit from continuing operations decreased by $0.3 million for the six months ended March 31, 2008 as compared to the six months ended March 31, 2007. The income tax provision of $39,183 for the six months ended March 31, 2008 relates to foreign income taxes incurred by Telecom FM. The Company did not have an income tax benefit for the six months ended March 31, 2008 as the Company has $13.5 million of net operating losses carryforwards which expire in 2026 and which are fully reserved. In addition, the Company does not have any net operating loss carrybacks.

Discontinued Operations:

	(dollars in thousands) For the Six Months Ended March 31, 2007
Percipia, Inc. Net loss	$ (308)
Pre-tax (loss) from discontinued operations	(308)
Income tax benefit	259
(Loss) from discontinued operations, net of income taxes	(49)
Gain on sale of assets from discontinued operations	2,183
Income tax (provision)	(822)
Gain on sale of assets from discontinued operations, net of income taxes	1,361
Income from discontinued operations, net of income taxes	$ 1,312

As indicated earlier, our significant divestitures have been recorded as discontinued operations:

On November 20, 2006, we closed a transaction to sell the real estate property associated with the previously sold high frequency radio business for $2.7 million in cash and a recognized gain in the amount of $2.2 million, $1.4 million net of income taxes.

On August 1, 2007, we sold all the outstanding shares of Percipia. The results of operations for the six months ended March 31, 2007 related to Percipia have been classified as discontinued operations.

Table of Contents

Liquidity and Capital Resources

Generally our working capital needs are funded from operations and advances under our revolving line of credit. In the lawn care and pest control business segment customers are billed when service is rendered and payment is usually received in less than thirty (30) days. In the telecommunication business segment customers are billed when orders are shipped and payment is usually received in sixty (60) to one hundred twenty (120) days from the billing date. Materials related to telecommunications equipment production must be purchased significantly in advance of the billing date and payment terms with vendors generally range between thirty (30) and sixty (60) days.

As of March 31, 2008, our liquidity and capital resources included cash and equivalents of $3.3 million, a working capital surplus of $0.4 million and $2.0 million was available under our revolving line of credit. As of September 30, 2007, our liquidity and capital resources included cash and equivalents of $2.8 million, a working capital deficit of $(0.9) million and $9.0 million available under our revolving line of credit.

Cash used in operating activities was $1.9 million for the six months ended March 31, 2008 as compared to cash provided by operating activities of $0.8 million for the six months ended March 31, 2007. During the six months ended March 31, 2008 the primary sources of cash from operating activities were increases in prepaid expenses of $0.5 million, increases in inventories of $0.2 million and an increase in customer deposits of $0.4 million. The primary uses of cash from operating activities for the six months ended March 31, 2008 were increase in accounts receivable of $1.2 million, reduction in accounts payable and accrued expenses of $0.8 million and funding of cash loss of $1.0 million.

Net cash used in investing activities was $1.3 million during the six months ended March 31, 2008 as compared to cash provided by investing activities of $0.6 million for the six months ended March 31, 2007. During the six months ended March 31, 2008 the primary uses of cash from investing activities were cash paid for the acquisition of Marshall of $1.0 million and capital expenditures of $0.3 million. For the six months ended March 31, 2007 the primary source of cash provided by investing activities was $2.5 million of net proceeds from the sale of assets offset by $1.5 million used for business acquisitions and $0.2 million used for the purchase of capital expenditures.

Net cash provided by financing activities was $3.7 million for the six months ended March 31, 2008 as compared to the repayment of debt of $1.0 million for the six months ended March 31, 2007. During the six months ended March 31, 2008 the primary source of cash from financing activities was proceeds from revolving line of credit of $3.8 million.

Cash flows from discontinued operations are included in the consolidated statement of cash flows within operating, investing and financing activities for the six months ended March 31, 2008 and 2007.

Our uses of cash for fiscal 2008 will be principally for working capital needs, capital expenditures and debt service. We are not anticipating significant acquisition activity in fiscal 2008. We believe that we can fund our planned business activities from a combination of cash flows from operations and funds available under our revolving line of credit. On February 12, 2008, we amended our revolving line of credit terms and conditions (the Second Amendment) which included an extension of the maturity date to January 7, 2009 from October 1, 2008, reduced the capacity under the credit agreement from $16.0 million to $13.5 million effective February 12, 2008, to $12.75 million as of June 30, 2008 and to $11.75 million as of September 30, 2008. The Second Amendment also modified the financial covenants relating to consolidated EBITDA, the leverage ratio and the fixed charge coverage ratio. Based on the revised financial covenants included in the Second Amendment, we were in compliance with the financial covenants in its revolving line of credit at March 31, 2008.

Table of Contents

Recent Accounting Pronouncements

See Note 2, Summary of Significant Accounting Policies in the Notes to the Condensed Consolidated Financial Statements for a discussion of recent accounting pronouncements and their effect, if any, on the Company.

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

Not applicable.

Item 4. ***Controls and Procedures***

(a) ***Evaluation of Disclosure Controls and Procedures***

As of the end of the period covered by this report, we conducted an evaluation, under the supervision and with the participation of our Chief Executive Officer and Chief Financial Officer of our disclosure controls and procedures (as defined in Rule 13a-15(e) and Rule 15d-15(e) of the Exchange Act). Based upon this evaluation, our Chief Executive Officer and Chief Financial Officer concluded that, at March 31, 2008, our disclosure controls and procedures are effective to ensure that information required to be disclosed by us in the reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the Commission s rules and forms.

(b) ***Changes in Internal Controls***

There was no change in our internal controls or in other factors that could affect these controls during the quarter ended March 31, 2008 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

Table of Contents

PART II
OTHER INFORMATION

Item 1. ***Legal Proceedings***

We are involved in litigation from time to time in the ordinary course of our business. Except for the litigation described below, we do not believe that any litigation in which we are currently involved, individually or in the aggregate, is material to our financial condition or results of operations.

In October 2007, the Company filed a lawsuit in the Circuit Court for the Ninth Judicial Circuit in the State of Florida against a number of former employees of Middleton for violation of their non-compete agreements. In addition, certain of these former employees pursued and hired away employees of Middleton which is also a violation of the existing employee non-compete agreements. The Company is seeking injunctive relief and damages. In October 2007, the Company also filed a lawsuit against a competitor for tortious interference alleging that they hired these former employees knowing that they were in violation of the Company s non-compete agreement. This matter was settled during the three months ended March 31, 2008 for an immaterial amount.

Item 1A. ***Risk Factors***

Not applicable.

Item 2. ***Unregistered Sales of Equity Securities and Use of Proceeds***

None.

Item 3. ***Defaults Upon Senior Securities***

None.

Item 4. ***Submission of Matters to a Vote of Security Holders***

The Company held its Annual Meeting of Shareholders on February 21, 2008. At the meeting, the following persons were elected to serve as directors, with the votes indicated:

Director	Affirmative Votes	Withheld Votes
Joseph Di Martino	8,650,805	2,488,683
Mario B. Ferrari	7,962,656	3,176,832
Arnold Heggestad, Ph. D.	8,651,805	2,487,683
Steven Oppenheim	8,650,270	2,489,218
Richard C. Rochon	7,963,156	3,176,332
Charles P. Steinmetz	7,963,121	3,176,367

Item 5. ***Other Information***

None.

Table of Contents

Item 6. ***Exhibits***

10.1	Second Amendment to the Credit Agreement dated as of February 12, 2008 by and among Sunair Services Corporation, its domestic subsidiaries from time to time parties thereto, the lenders parties thereto and Wachovia Bank, National Association as administrative agent for the lenders (incorporated by reference to Exhibit 10.1 in the Form 8-K filed with the SEC on February 15, 2008).
31.1	Certification by Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002*
31.2	Certification by Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002*
32.1	Certification by Chief Executive Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002*
32.2	Certification by Chief Financial Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002*

* Filed herewith

Table of Contents

SIGNATURES

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

SUNAIR SERVICES CORPORATION

Date: May 15, 2008

/s/ John J. Hayes
John J. Hayes
President and Chief Executive Officer

Date: May 15, 2008

/s/ Edward M. Carriero, Jr.
Edward M. Carriero, Jr.
Chief Financial Officer

: 10pt">

our ability to generate revenues or achieve or maintain profitability;

the future revenues and profitability of our potential customers, suppliers and collaborators; and

the availability to us of capital.

If we are successful in obtaining FDA approval for Exelbine, it will compete with Navelbine, its generic equivalents and other formulations of vinorelbine that may be approved by the FDA. Our ability to commercialize Exelbine will depend in part on the extent to which governmental authorities, private health insurers and other organizations establish what we believe are appropriate coverage and reimbursement levels for the cost of our product. These payors are increasingly attempting to contain healthcare costs by limiting both coverage and the level of reimbursement, particularly for new therapeutic products or if there is a perception that the target indication of the new product is well-served by existing drugs or other treatments. Accordingly, even if coverage and reimbursement are provided, market acceptance of our products would be adversely affected if the amount of coverage and/or reimbursement rates for the use of our products proved to be unprofitable for healthcare providers or less profitable than alternative treatments.

Table of Contents

There have been federal and state proposals to subject the pricing of healthcare goods and services to government control and to make other changes to the U.S. healthcare system. While we cannot predict the outcome of current or future legislation, we anticipate, particularly given the passage in 2010 of the Patient Protection and Affordable Care Act, that Congress and state legislatures will introduce initiatives directed at lowering the total cost of healthcare. In addition, in certain foreign markets, the pricing of drug products is subject to government control and reimbursement may in some cases be unavailable or insufficient. It is uncertain if future legislative proposals, whether domestic or abroad, will be adopted that might affect our products or product candidates or what actions federal, state, or private payors for healthcare treatment and services may take in response to any such healthcare reform proposals or legislation. Any such healthcare reforms could have a material and adverse effect on the marketability of any products for which we ultimately receive FDA or other regulatory agency approval.

We face potential product liability exposure and, if successful claims are brought against us, we may incur substantial liability for a product or product candidate and may have to limit its commercialization. In the future, we anticipate that we will need to obtain additional or increased product liability insurance coverage and it is uncertain that such increased or additional insurance coverage can be obtained on commercially reasonable terms, if at all.

Our business (in particular, the use of our product candidates in clinical trials and the sale of any products for which we obtain marketing approval) will expose us to product liability risks. Product liability claims might be brought against us by patients, healthcare providers, pharmaceutical companies or others selling our products. If we cannot successfully defend ourselves against any such claims, we will incur substantial liabilities. Regardless of merit or eventual outcome, liability claims may result in:

decreased demand for our products;
impairment of our business reputation;
withdrawal of bioequivalence or clinical trial participants;
costs of related litigation;
substantial monetary awards to patients or other claimants;
loss of revenues; and
the inability to commercialize our products and product candidates.

We maintain limited product liability insurance for our bioequivalence and clinical trials, but our insurance coverage may not reimburse us or may not be sufficient to reimburse us for all expenses or losses we may suffer. Moreover, insurance coverage is becoming increasingly expensive and, in the future, we may not be able to maintain insurance coverage at a reasonable cost or in sufficient amounts to protect us against losses.

We expect that we would expand our insurance coverage to include the sale of commercial products if we obtain marketing approval of any of our product candidates, but we may be unable to obtain product liability insurance on commercially acceptable terms or may not be able to maintain such insurance at a reasonable cost or in sufficient amounts to protect us against potential losses. Large judgments have been awarded in class action lawsuits based on drug products that had unanticipated side effects. A successful product liability claim or series of claims brought against us could cause our stock price to fall and, if judgments exceed our insurance coverage, could decrease our cash and adversely affect our business.

RISKS RELATED TO OUR COMMON STOCK

If we are unable to maintain compliance with NYSE Amex continued listing standards, we may be delisted from the NYSE Amex equities market, which would likely cause the liquidity and market price of our common stock to decline.

Our common stock currently is listed on the NYSE Amex equities market. The NYSE Amex normally will consider suspending dealings in, or removing from the list, securities of an issuer that has stockholders equity of less than $6.0 million if such issuer has sustained losses from continuing operations and/or net losses in its five most recent fiscal years. In addition, the NYSE Amex will normally consider suspending dealings in, or removing from the list, securities selling for a substantial period of time at a low price per share if the issuer fails to effect a reverse split of such stock within a reasonable time after being notified that the NYSE Amex deems such action to be appropriate under the circumstances.

-44-

Table of Contents

Previously, we were not in compliance with certain NYSE Amex stockholders equity continued listing standards. Specifically, we were not in compliance with (1) Section 1003(a)(ii) of the NYSE Amex Company Guide, or the Company Guide, because we reported stockholders equity of less than $4,000,000 and losses from continuing operations and net losses in three of our four most recent fiscal years, or (2) Section 1003(a)(iii) of the Company Guide, because we reported stockholders equity of less than $6,000,000 and losses from continuing operations and net losses in our five most recent fiscal years. In addition, we were notified, in accordance with Section 1003(f)(v) of the Company Guide, that the NYSE Amex determined it was appropriate for us to effect a reverse stock split of our common stock to address our low selling price per share.

In April 2010, we announced that we had resolved the stockholders equity continued listing deficiencies and we implemented a 1-for-25 reverse split of our common stock, in part to address the NYSE Amex s requirement that we address our low stock price. Even though, currently, we are in compliance with NYSE Amex continued listing standards, there is no assurance that we will continue to maintain compliance with such standards. For example, we may determine to grow our organization or product pipeline or pursue development or other activities at levels or on timelines that reduces our stockholders equity below the level required to maintain compliance with NYSE Amex continued listing standards. In addition, the market price for our common stock historically has been highly volatile, as more fully described below under the risk titled The market price of our common stock historically has been and likely will continue to be highly volatile. The NYSE Amex may again determine that the selling price per share of our common stock is low and require that we effect a reverse stock split of our common stock, which would require stockholder approval that we may be unable to obtain. Our failure to maintain compliance with NYSE Amex continued listing standards could result in the delisting of our common stock from the NYSE Amex.

The delisting of our common stock from the NYSE Amex likely would reduce the trading volume and liquidity in our common stock and may lead to decreases in the trading price of our common stock. The delisting of our common stock may also materially impair our stockholders ability to buy and sell shares of our common stock. In addition, the delisting of our common stock could significantly impair our ability to raise capital, which is critical to the execution of our current business strategy.

If our common stock were delisted and determined to be a penny stock, a broker-dealer may find it more difficult to trade our common stock and an investor may find it more difficult to acquire or dispose of our common stock in the secondary market.

If our common stock were removed from listing with the NYSE Amex, it may be subject to the so-called penny stock rules. The SEC has adopted regulations that define a penny stock to be any equity security that has a market price per share of less than $5.00, subject to certain exceptions, such as any securities listed on a national securities exchange. For any transaction involving a penny stock, unless exempt, the rules impose additional sales practice requirements on broker-dealers, subject to certain exceptions. If our common stock were delisted and determined to be a penny stock, a broker-dealer may find it more difficult to trade our common stock and an investor may find it more difficult to acquire or dispose of our common stock on the secondary market.

The market price of our common stock historically has been and likely will continue to be highly volatile.

The market price for our common stock historically has been highly volatile, and the market for our common stock has from time to time experienced significant price and volume fluctuations that are unrelated to our operating performance. For instance, on October 1, 2007, the market price for our common stock dropped almost 80% following our announcement of the results of our phase 2b clinical trial of CoFactor for the first-line treatment of metastatic colorectal cancer. Conversely, the market price for our common stock more than doubled over two trading days in late December 2009. The market price of our common stock may fluctuate significantly in response to a number of factors, including:

- the level of our financial resources;
- announcements of entry into or consummation of a financing or strategic transaction;

Table of Contents

changes in the regulatory status of our product candidates, including results of any bioequivalence and clinical trials and other research and development programs;

FDA or international regulatory actions and regulatory developments in the U.S. and foreign countries;

announcements of new products or technologies, commercial relationships or other events (including bioequivalence and clinical trial results and regulatory events and actions) by us or our competitors;

market conditions in the pharmaceutical, biopharmaceutical, specialty pharmaceutical and biotechnology sectors;

developments concerning intellectual property rights generally or those of us or our competitors;

changes in securities analysts estimates of our financial performance or deviations in our business and the trading price of our common stock from the estimates of securities analysts;

events affecting any future collaborations, commercial agreements and grants;

fluctuations in stock market prices and trading volumes of similar companies;

sales of large blocks of our common stock, including sales by our executive officers, directors and significant stockholders or pursuant to shelf or resale registration statements that register shares of our common stock that may be sold by us or certain of our current or future stockholders;

discussion of us or our stock price by the financial and scientific press and in online investor communities;

commencement of delisting proceedings by the NYSE Amex;

additions or departures of key personnel; and

changes in third-party payor reimbursement policies.

As evidenced by the October 1, 2007 decline, the realization of any of the foregoing could have a dramatic and adverse impact on the market price of our common stock. In addition, class action litigation has often been instituted against companies whose securities have experienced substantial decline in market price. Moreover, regulatory entities often undertake investigations of investor transactions in securities that experience volatility following an announcement of a significant event or condition. Any such litigation brought against us or any such investigation involving our investors could result in substantial costs and a diversion of management s attention and resources, which could hurt our business, operating results and financial condition.

Sales of substantial amounts of our common stock or the perception that such sales may occur could cause the market price of our common stock to drop significantly, even if our business is performing well.

The market price of our common stock could decline as a result of sales by, or the perceived possibility of sales by, us or our existing stockholders of shares of our common stock. These sales by our existing stockholders might also make it more difficult for us to sell equity securities at a time and price that we deem appropriate. Currently, we have an effective primary registration statement on Form S-3 under which we may sell and issue more than $85 million of securities. In addition, we have effective resale registration statements on Form S-3 and an effective registration statement on Form S-1 that register a significant number of shares of our common stock and securities convertible into our common stock that may be sold by us or certain of our stockholders. Collectively, these registration statements may increase the likelihood of sales by, or the perception of an increased likelihood of sales by, us or our existing stockholders of shares of our common stock.

Table of Contents

If our acquisition of SynthRx closes, we may obtain voting control over a significant amount of our outstanding common stock and we may determine to cause those shares to be voted in such a manner that does not necessarily coincide with the interests of individual stockholders or particular groups of stockholders.

Pursuant to the voting and transfer restriction agreement between us and each of the other parties thereto, each other party has agreed to vote all shares of our common stock beneficially owned by that party with respect to every action or approval by written consent of our stockholders in such manner as directed by us, except in limited circumstances, and has executed an irrevocable proxy appointing and authorizing us to vote such shares in such manner. If our acquisition of SynthRx closes we will issue 2,938,773 shares of our common stock to SynthRx s stakeholders, representing, in the aggregate, approximately 11% of our company (based on our currently outstanding shares plus shares issued in connection with the closing). If our acquisition of SynthRx closes, our stockholders approve the issuance of the milestone-related shares and development of purified 188 achieves all related milestones without reduction, we will issue an additional 13,478,050 shares of our common stock, representing, in the aggregate (and including the shares issued in connection with the closing) an approximately 40% ownership stake in our company (based on our currently outstanding shares plus shares issued in connection with the acquisition). As a result of such issuances and the voting and transfer restriction agreement, we may, at and following the closing of the acquisition, have significant control over substantially all matters requiring approval by our stockholders, including the election of directors and the approval of certain mergers and other business combination transactions. Even if less than all potential milestone-related shares are issued, our ability to control a potentially significant block of stockholder votes pursuant to the voting and transfer restriction agreement may enable us to substantially affect the outcome of proposals brought before our stockholders. Although our board of directors acts in a manner it believes is in the best interest of our stockholders as a whole, the interests of our stockholders as a whole may not always coincide with the interests of individual stockholders or particular groups of stockholders.

Anti-takeover provisions in our charter documents and under Delaware law may make an acquisition of us, which may be beneficial to our stockholders, more difficult, which could depress our stock price. Alternatively, prohibitions on anti-takeover provisions in our charter documents may restrict us from acting in the best interests of our stockholders.

We are incorporated in Delaware. Certain anti-takeover provisions of Delaware law and our charter documents as currently in effect may make a change in control of our company more difficult, even if a change in control would be beneficial to our stockholders. Our bylaws limit who may call a special meeting of stockholders and establish advance notice requirements for nomination of individuals for election to our board of directors or for proposing matters that can be acted upon at stockholders meetings. Delaware law also prohibits corporations from engaging in a business combination with any holders of 15% or more of their capital stock until the holder has held the stock for three years unless, among other possibilities, the board of directors approves the transaction. Our board of directors may use these provisions to prevent changes in the management and control of our company. Also, under applicable Delaware law, our board of directors may adopt additional anti-takeover measures in the future. In addition, provisions of certain compensatory contracts with our management, such as equity award agreements, may have an anti-takeover effect by resulting in accelerated vesting of outstanding equity securities held by our executive officers. In particular, in the event of a change in control, the vesting of options we granted since July 2009 to our current executives will accelerate with respect to fifty percent of the then unvested shares on the day prior to the date of the change in control and, subject to the respective executive s continuous service, with respect to the remaining fifty percent of the then unvested shares on the one year anniversary of the date of the change in control. As a result, if an acquirer desired to retain the services of one or both of our current executives following an acquisition, it may be required to provide additional incentive to them, which could increase the cost of the acquisition to the acquirer and may deter or affect the terms of the potential acquisition.

In connection with a July 2005 private placement, we agreed with the investors in that transaction that we would not implement certain additional measures that would have an anti-takeover effect. As a result, under our amended and restated certificate of incorporation, we are prohibited from dividing our board of directors into classes and adopting or approving any rights plan, poison pill or other similar plan or device. A classified board of directors could serve to protect our stockholders against unfair treatment in takeover situations, by making it more difficult and

time-consuming for a potential acquirer to take control of our board of directors. A company may also adopt a classified board of directors to ensure stability in the board of directors and thereby improve long-term planning, which may benefit stockholders. A poison pill or similar plan or device may encourage potential acquirers to discuss their intentions with the board of directors of a company and avoid the time, expense and distraction of a hostile take-over. Any benefit to us and our stockholders from instituting a classified board or adopting or approving a poison pill or similar plan or device in these and other circumstances is unavailable.

Table of Contents

Because we do not expect to pay dividends with respect to our common stock in the foreseeable future, you must rely on stock appreciation for any return on your investment.

We have paid no cash dividends on any of our common stock to date, and we currently intend to retain our future earnings, if any, to fund the development and growth of our business. As a result, with respect to our common stock, we do not expect to pay any cash dividends in the foreseeable future, and payment of cash dividends, if any, will also depend on our financial condition, results of operations, capital requirements and other factors and will be at the discretion of our board of directors. Furthermore, we are subject to various laws and regulations that may restrict our ability to pay dividends and we may in the future become subject to contractual restrictions on, or prohibitions against, the payment of dividends. Due to our intent to retain any future earnings rather than pay cash dividends on our common stock and applicable laws, regulations and contractual obligations that may restrict our ability to pay dividends on our common stock, the success of your investment in our common stock will likely depend entirely upon any future appreciation and there is no guarantee that our common stock will appreciate in value.

Item 1B. Unresolved Staff Comments.

We do not have any unresolved comments issued by the SEC staff.

Item 2. Properties.

We lease approximately 6,500 square feet of office space for our headquarters in San Diego, California subject to a lease arrangement that will expire in January 2012, unless we exercise our option to extend the lease for an additional 12 months. The average base rent for this space is approximately $15,600 per month. We believe that the facilities we lease are adequate to meet our current requirements and our requirements for the remaining term of the lease. We have no laboratory, research or manufacturing facilities.

Item 3. Legal Proceedings.

In the normal course of business, we may become subject to lawsuits and other claims and proceedings. Such matters are subject to uncertainty and outcomes are often not predictable with assurance. We are not currently a party to any material pending litigation or other material legal proceeding.

Item 4. (Removed and Reserved).

Table of Contents

PART II

Item 5. Market for Registrant s Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities.

Market Information

Our common stock trades under the symbol ANX on NYSE Amex Equities. The following table sets forth the high and low closing sale prices for our common stock in each full quarterly period within the two most recent fiscal years as reported in the consolidated transaction reporting system for NYSE Amex Equities. The prices in the table below have been adjusted to reflect retrospective application of the 1-for-25 reverse split of our common stock effected on April 23, 2010.

	Closing Sale Price			
	2010		2009	
	High	Low	High	Low
First Quarter	$ 11.67	$ 5.00	$ 4.50	$ 2.25
Second Quarter	$ 6.80	$ 1.61	$ 5.50	$ 2.76
Third Quarter	$ 2.11	$ 1.53	$ 5.00	$ 3.00
Fourth Quarter	$ 2.99	$ 1.93	$ 10.75	$ 2.25

As of March 1, 2011, we had approximately 143 record holders of our common stock. We believe that the number of beneficial owners is substantially greater than the number of record holders because a large portion of our common stock is held of record through brokerage firms in street name.

Dividend Policy

We have never declared or paid any cash dividends on our common stock and do not anticipate declaring or paying any cash dividends on our common stock in the foreseeable future. In addition, in connection with previous preferred stock financings, we have agreed to charter restrictions on our ability to pay cash dividends or distributions on our common stock for so long as any shares of such preferred stock are outstanding, unless we obtain prior written consent from the holders of such preferred stock. Although currently there are no such restrictions on our ability to pay dividends on our common stock, we may agree to similar restrictions in the future.

We expect to retain all available funds and any future earnings to support operations and fund the development and growth of our business. Our board of directors will determine whether we pay and the amount of future dividends (including cash dividends), if any.

Recent Sales of Unregistered Securities

As partial consideration for its services as placement agent in connection with registered direct offerings of our equity securities, we have issued the following common stock purchase warrants to Rodman & Renshaw, LLC, or its designee, on the dates indicated:

- on June 12, 2009, warrants to purchase an aggregate of up to 36,071 shares of our common stock at an exercise price of $3.75 per share, which warrants became exercisable on December 13, 2009 and may be exercised any time on or before June 12, 2014;
- on July 6, 2009, warrants to purchase an aggregate of up to 19,007 shares of our common stock at an exercise price of $4.475 per share, which warrants became exercisable on January 7, 2010 and may be exercised any time on or before July 6, 2014;

Table of Contents

on August 10, 2009, warrants to purchase an aggregate of up to 14,183 shares of our common stock at an exercise price of $4.0625 per share, which warrants became exercisable on February 10, 2010 and may be exercised any time beginning on or before August 10, 2014;

on October 9, 2009, warrants to purchase an aggregate of up to 144,000 shares of our common stock at an exercise price of $5.875 per share, which warrants became exercisable on April 7, 2010 and may be exercised any time on or before October 6, 2014;

on January 7, 2010, warrants to purchase an aggregate of up to 99,696 shares of our common stock at an exercise price of $11.9125 per share, which warrants became exercisable on July 7, 2010 and may be exercised any time on or before June 3, 2014; and

on January 11, 2011, warrants to purchase an aggregate of up to 409,228 shares of our common stock at an exercise price of $3.44 per share, which warrants were exercisable upon issuance and may be exercised any time on or before April 1, 2015.

The warrants described above were offered and sold by us in reliance upon exemptions from the registration statement requirements by Section 4(2) of the Securities Act of 1933, as amended, as transactions by an issuer not involving a public offering. The number of underlying shares and exercise prices of the warrants described above that were issued prior to April 23, 2010 have been adjusted to reflect retrospective application of the 1-for-25 reverse split of our common stock effected on April 23, 2010.

Item 6. Selected Financial Data.

Under SEC rules and regulations, as a smaller reporting company we are not required to provide the information required by this item.

Item 7. Management s Discussion and Analysis of Financial Condition and Results of Operations.

The following discussion and analysis of our financial condition and results of operations should be read in conjunction with the consolidated financial statements and related notes appearing elsewhere in this report. In addition to historical information, this discussion and analysis contains forward-looking statements that involve risks, uncertainties, and assumptions. Our actual results may differ materially from those anticipated in these forward-looking statements as a result of certain factors, including but not limited to those identified under Item 1A Risk Factors in this report.

Overview

We are a specialty pharmaceutical company focused on acquiring, developing and commercializing proprietary product candidates. Our lead product candidates, Exelbine (vinorelbine injectable emulsion), or ANX-530, and ANX-514 (docetaxel emulsion for injection), are novel emulsion formulations of currently marketed chemotherapy drugs.

We have devoted substantially all of our resources to research and development, or R&D, or to acquisition of our product candidates. We have not yet marketed or sold any products or generated any significant revenue and we have incurred significant losses since inception. We had a loss from operations of $8.5 million for the year ended December 31, 2010 and cash of approximately $28.0 million at December 31, 2010.

In November 2010, we submitted a new drug application, or NDA, for Exelbine to the U.S. Food and Drug Administration, or FDA, and in January 2011, we announced that the FDA accepted the Exelbine NDA for filing and established a Prescription Drug User Fee Act, or PDUFA, goal date of September 1, 2011 to finish its review of the Exelbine NDA.

In February 2011, we met with the FDA to discuss ANX-514 and the data package we presented to FDA to support approval of ANX-514 based on data from our bioequivalence study of ANX-514. The FDA indicated that a randomized safety study comparing ANX-514 and Taxotere would be required to support approval of ANX-514. The study would be primarily descriptive but with a sample size sufficient to demonstrate a comparable safety profile. The FDA recommended that the study also collect data on response rate and duration of response. We are developing a study protocol for submission to the FDA and intend to continue discussions with the FDA regarding the phase 3 clinical study and requirements for ANX-514 s approval.

Table of Contents

In 2010, we additionally began to focus on expanding our product pipeline through one or more in-license, asset acquisition or merger transactions. In February 2011, we entered into an agreement and plan of merger to acquire SynthRx, Inc., a privately-held Delaware corporation developing a purified form of a rheologic and antithrombotic agent, poloxamer 188, or 188, in exchange for shares of our common stock. We expect to consummate the acquisition of SynthRx in the first half of 2011. As discussed in more detail under Part I, Item 1 Business in this report, we initially intend to develop purified 188 for the treatment of sickle cell crisis in a pediatric population and, if our acquisition of SynthRx closes and we are able to reach agreement with the FDA on a study protocol on a timely basis, we may initiate a phase 3 clinical trial of purified 188 for that indication in 2012. In connection with the consummation of this acquisition, we would issue 2,938,773 shares of our common stock to SynthRx s stakeholders, 1,938,773 of which would be subject to repurchase by us in the event development of purified 188 does not achieve the first milestone described below. We could issue up to an aggregate of 13,478,050 additional shares of our common stock to SynthRx s stakeholders if the development of purified 188 achieves certain milestones, as described below, and our stockholders approve the issuance of such milestone-related shares, as required by NYSE Amex rules. If our stockholders do not approve the issuance of the milestone-related shares, under the terms of the merger agreement, we would be required to pay SynthRx s stakeholders in cash the value of the milestone-related shares we would have otherwise issued, with all such cash payments made in quarterly installments and, with respect to the cash value associated with 12,478,050 of the milestone-related shares, payable based on net sales of purified 188. We cannot determine the amount of our potential cash payments to SynthRx s stakeholders because the amount of such payments, if any, will depend on the 10-day volume weighted average of the closing price of our common stock at the time a milestone is achieved and the market price of our common stock historically has been, and likely will continue to be, highly volatile. Of the shares issuable in connection with achievement of milestones, up to 1,000,000 shares would be issuable upon the dosing of the first patient in a phase 3 clinical study that the FDA has indicated may be sufficient to support approval of a new drug application covering the use of purified 188 for the treatment of sickle cell crisis in children, or the 188 NDA, which we refer to as the First Milestone; 3,839,400 shares would be issuable upon acceptance for review of the 188 NDA by the FDA, which we refer to as the Second Milestone; and 8,638,650 shares would be issuable upon approval by the FDA of the 188 NDA, which we refer to as the Third Milestone.

We anticipate that our cash as of December 31, 2010, together with net proceeds from the equity financing we completed in January 2011, will be sufficient to fund our currently planned level of operations for at least the next 12 months. However, we may pursue development and/or commercialization activities for our current or future product candidates, including purified 188 should we consummate the acquisition of SynthRx, at levels or on timelines, or we may incur unexpected expenses, that shorten the period through which our operating funds will sustain us. We may also acquire new technologies, product candidates and/or products and the cost to acquire, develop and/or commercialize such new technologies, product candidates and/or products may shorten the period through which our operating funds will sustain us. In addition, we may seek to raise substantial additional capital to support activities that we believe will enhance the value of our programs and increase stockholder value. We may not be able to obtain additional financing on a timely basis or on acceptable terms, if at all.

Recent Financings

In 2010, we raised an aggregate of $27.4 million in adjusted net proceeds through the issuance and sale of units consisting of convertible preferred stock and warrants to purchase shares of our common stock, and, in January 2011, we raised an additional $21.0 million in net proceeds through the issuance and sale of units consisting of common stock and warrants to purchase common stock as follows:

- In January 2010, we completed a registered direct equity financing involving the issuance of units consisting of shares of our 3.73344597664961% Series E Convertible Preferred Stock, or Series E Stock, which were convertible into an aggregate of 1,993,965 shares of our common stock, and 30-month warrants to purchase up to an aggregate of 498,488 shares of our common stock. The gross proceeds of this financing were $19.0 million, and we received $14.0 million in net proceeds after deducting amounts deposited into escrow accounts to fund our dividend and related payment obligations in respect of the Series E Stock, the fees and expenses of our placement agent, and our other offering expenses. All of the shares of our Series E Stock have been converted into common stock and are no

longer outstanding. We may receive up to $4.4 million of additional proceeds from the exercise of the warrants issued in this financing. Those warrants have an exercise price of $8.75 per share and are exercisable any time on or before July 6, 2012, subject to certain beneficial ownership limitations.

Table of Contents

In May 2010, we completed a registered direct equity financing involving the issuance of units consisting of shares of our 2.19446320054018% Series F Convertible Preferred Stock, or Series F Stock, which were convertible into an aggregate of 5,190,312 shares of our common stock, 5-year warrants to purchase up to an aggregate of 1,816,608 shares of our common stock and 1-year warrants to purchase up to an aggregate of 778,548 shares of our common stock. The gross proceeds of this financing were $19.2 million, and we received $13.3 million in net proceeds after deducting amounts deposited into escrow accounts to fund our dividend and related payment obligations in respect of the Series F Stock, the fees and expenses of our placement agent and financial advisor, and our other offering expenses. All of the shares of our Series F Stock have been converted into common stock and are no longer outstanding. We may receive up to $9.5 million of additional proceeds from the exercise of the warrants issued in this financing. Those warrants have an exercise price of $3.65 per share. The 5-year warrants are exercisable any time on or before May 6, 2015 and the 1-year warrants are exercisable any time on or before May 20, 2011, subject to certain beneficial ownership limitations.

In January 2011, we completed a registered direct equity financing involving the issuance of units consisting of 8,184,556 shares of our common stock, 5-year warrants to purchase up to an aggregate of 2,046,139 shares of our common stock and 1-year warrants to purchase up to an aggregate of 2,046,139 shares of our common stock. The gross proceeds of this financing were $22.5 million, and we received $21.0 million in net proceeds after deducting the fees and expenses of our placement agent and our other offering expenses. We may receive up to $11.3 million of additional proceeds from the exercise of the warrants issued in this financing. Those warrants have an exercise price of $2.75 per share. The 5-year warrants are exercisable any time on or before January 11, 2016 and the 1-year warrants are exercisable any time on or before January 19, 2012, subject to certain beneficial ownership limitations.

Reverse Stock Split

On April 23, 2010, we effected a 1-for-25 reverse split of our common stock, which was authorized by our stockholders at a special meeting held in August 2009. The reverse stock split reduced the number of our issued and outstanding shares of common stock as of April 23, 2010 from approximately 257.3 million shares to approximately 10.3 million shares. All common stock share and per share information included in this report have been restated to reflect retrospective application of the reverse stock split for periods ending or as of a date prior to April 23, 2010, except for par value per share and the number of authorized shares, which were not affected by the reverse stock split.

Critical Accounting Policies and Estimates

Our discussion and analysis of our financial condition and results of operations is based upon consolidated financial statements that we have prepared in accordance with accounting principles generally accepted in the U.S. The preparation of these financial statements requires management to make a number of assumptions and estimates that affect the reported amounts of assets, liabilities, revenues and expenses in these consolidated financial statements and accompanying notes. On an on-going basis, we evaluate these estimates and assumptions, including those related to recognition of expenses in service contracts, license agreements and share-based compensation. Management bases its estimates on historical information and assumptions believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions.

Table of Contents

Revenue Recognition. We may enter into revenue arrangements that contain multiple deliverables. In these cases, revenue is recognized when all of the following criteria are met: (1) persuasive evidence of an arrangement exists; (2) delivery has occurred or services have been rendered; (3) the seller s price to the buyer is fixed and determinable; and (4) collectability is reasonably assured.

Revenue from licensing agreements is recognized based on the performance requirements of the agreement. Revenue is deferred for fees received before earned. Nonrefundable upfront fees that are not contingent on any future performance by us are recognized as revenue when the license term commences and the revenue recognition criteria are met. Nonrefundable upfront fees, where we have ongoing involvement or performance obligations, are recorded as deferred revenue and recognized as revenue over the life of the contract, the period of the performance obligation or the development period, whichever is appropriate in light of the circumstances.

Payments related to substantive, performance-based milestones in an agreement are recognized as revenue upon the achievement of the milestones as specified in the underlying agreement when they represent the culmination of the earnings process. Royalty revenue from licensed products will be recognized when earned in accordance with the terms of the applicable license agreements.

We recognize revenues from federal government research grants during the period in which we receive the grant funds, or their collection is reasonably assured, and we incur the qualified expenditures.

R&D Expenses. R&D expenses consist of expenses incurred in performing R&D activities, including salaries and benefits, facilities and other overhead expenses, bioequivalence and clinical trials, research-related manufacturing services, contract services and other outside expenses. R&D expenses are charged to operations as the underlying work is performed. Advance payments, including nonrefundable amounts, for goods or services that will be used or rendered for future R&D activities are deferred and capitalized. Such amounts will be recognized as an expense as the related goods are delivered or the related services are performed. If the goods will not be delivered, or services will not be rendered, then the capitalized advance payment is charged to expense.

Milestone payments that we make in connection with in-licensed technology or product candidates are expensed as incurred when there is uncertainty in receiving future economic benefits from the licensed technology or product candidates. We consider the future economic benefits from the licensed technology or product candidates to be uncertain until such licensed technology is incorporated into products that, or such product candidates, are approved for marketing by the FDA or when other significant risk factors are abated. For accounting purposes, management has viewed future economic benefits for all of our licensed technology or product candidates to be uncertain.

Payments in connection with our bioequivalence and clinical trials are often made under contracts with multiple contract research organizations that conduct and manage these trials on our behalf. The financial terms of these agreements are subject to negotiation and vary from contract to contract and may result in uneven payment flows. Generally, these agreements set forth the scope of work to be performed at a fixed fee or unit price or on a time-and-material basis. Payments under these contracts depend on factors such as the successful enrollment or treatment of patients or the completion of other milestones. Expenses related to bioequivalence and clinical trials are accrued based on our estimates and/or representations from service providers regarding work performed, including actual level of patient enrollment, completion of patient studies, and trial progress. Other incidental costs related to patient enrollment or treatment are accrued when reasonably certain. If the contracted amounts are modified (for instance, as a result of changes in the bioequivalence or clinical trial protocol or scope of work to be performed), we modify our accruals accordingly on a prospective basis. Revisions in scope of contract are charged to expense in the period in which the facts that give rise to the revision become reasonably certain. Because of the uncertainty of possible future changes to the scope of work in bioequivalence and clinical trials contracts, we are unable to quantify an estimate of the reasonably likely effect of any such changes on our consolidated results of operations or financial position. Historically, we have had no material changes in our bioequivalence and clinical trial expense accruals that would have had a material impact on our consolidated results of operations or financial position.

Purchased In-Process Research and Development. We adopted the Financial Accounting Standards Board s, or FASB s, changes to Accounting Standards Codification, or ASC, 805, Business Combinations, effective January 1, 2009. The adoption of the changes to ASC 805 did not have a material effect on our consolidated results of operations or financial position.

Table of Contents

In accordance with previous accounting guidance effective through December 31, 2008, we accounted for the costs associated with any purchased in-process research and development, or IPR&D, as an expense on the statement of operations upon acquisition. These amounts represented an estimate of the fair value of purchased IPR&D for projects that, as of the acquisition date, had not yet reached technological feasibility, had no alternative future use, and had uncertainty in generating future economic benefits. We determined the future economic benefits from the purchased IPR&D to be uncertain until such technology is incorporated into products approved for marketing by the FDA or when other significant risk factors are abated.

Share-based Compensation Expenses. We account for share-based compensation awards granted to employees, including non-employee members of our board of directors, in accordance with ASC 718, Compensation Stock Compensation. Share-based compensation expense is measured at the grant date, based on the estimated fair value of the award, and is recognized as expense over the employee s requisite service period. As share-based compensation expense is based on awards ultimately expected to vest, it has been reduced for estimated forfeitures. ASC 718 requires forfeitures to be estimated at the time of grant and revised, if necessary, in subsequent periods if actual forfeitures differ from those estimates. Forfeitures are estimated based on historical experience. Although estimates of share-based compensation expenses are significant to our consolidated financial statements, they are not related to the payment of any cash by us.

We estimate the fair value of stock option awards on the date of grant using the Black-Scholes option-pricing model, or Black-Scholes model. The determination of the fair value of share-based payment awards on the date of grant using an option-pricing model is affected by the price of our common stock as well as assumptions regarding a number of complex and subjective variables. These variables include, but are not limited to, our expected share price volatility over the term of the awards, actual and projected employee stock option exercise behaviors, a risk-free interest rate and expected dividends. We may elect to use different assumptions under the Black-Scholes model in the future, which could materially affect our net income or loss and net income or loss per share.

We account for share-based compensation awards granted to non-employees by determining the fair value of the share-based compensation awards granted as either the fair value of the consideration received or the fair value of the equity instruments issued, whichever is more reliably measurable. If the fair value of the equity instruments issued is used, it is measured using the share price and other measurement assumptions as of the earlier of (1) the date at which a commitment for performance by the counterparty to earn the equity instruments is reached or (2) the date at which the counterparty s performance is complete.

Income Taxes. We account for income taxes and the related accounts under the liability method in accordance with ASC 740, Income Taxes. Deferred tax assets and liabilities are determined based on the differences between the financial statement carrying amounts and the income tax bases of assets and liabilities. A valuation allowance is applied against any net deferred tax asset if, based on available evidence, it is more likely than not that some or all of the deferred tax assets will not be realized.

The tax effects from an uncertain tax position can be recognized in our consolidated financial statements only if the position is more likely than not of being sustained upon an examination by tax authorities. An uncertain income tax position will not be recognized if it has less than a 50% likelihood of being sustained.

Costs Associated with Exit or Disposal Activities. As part of our efforts to reduce operating costs, we completed one workforce reduction in the fourth quarter of 2008 and two workforce reductions in the first six months of 2009, each of which was accounted for in accordance with ASC 420, Exit or Disposal Cost Obligations. We recorded severance-related charges, including salary, payroll taxes and healthcare benefits, of $757,000 in the aggregate over three consecutive quarters beginning in the fourth quarter of 2008. We recorded severance-related charges of $350,000 in the first quarter of 2009, of which $237,000 was recorded in research and development and the balance was recorded in selling, general and administrative, and $163,000 in the second quarter of 2009, of which $121,000 was recorded in research and development and the balance was recorded in selling, general and administrative. As of June 30, 2009, all severance-related costs associated with these workforce reductions had been recorded and paid.

Table of Contents

Convertible Instruments. At issuance, we value separately embedded beneficial conversion features present in convertible securities. Embedded beneficial conversion features are recognized by allocating to additional paid-in capital and accumulated deficit that portion of the net proceeds from the sale of the convertible security equal to the intrinsic value of the beneficial conversion feature. Intrinsic value is calculated as the difference, as of the commitment date, between the conversion price of the convertible security and the fair value of the common stock underlying the convertible security, which for us is the closing price of a share of our common stock on the NYSE Amex multiplied by the number of shares of our common stock into which the convertible security is convertible. If the intrinsic value of the beneficial conversion feature is greater than the net proceeds allocated to the convertible security, the amount of the discount assigned to the beneficial conversion feature is limited to the amount of the net proceeds. In our registered direct equity financings that closed in June, July, August and October 2009 and January and May 2010, we issued convertible preferred stock securities with non-detachable conversion features that were in-the-money as of the commitment date, which we recognized as beneficial conversion features. All of the shares of the convertible preferred stock we issued in these financings have been converted into common stock at fixed conversion rates. The embedded beneficial conversion features were valued separately and recognized by allocating to additional paid-in capital and accumulated deficit a portion of the net proceeds equal to the intrinsic value of the beneficial conversion features.

The foregoing is not intended to be a comprehensive list of all of our accounting policies. In most cases, the accounting treatment of a particular transaction is specifically dictated by accounting principles generally accepted in the U.S.

Results of Operations

A general understanding of the drug development process is critical to understanding our results of operations. Drug development in the U.S. and most countries throughout the world is a process that includes several steps defined by the FDA and similar regulatory authorities in foreign countries. The FDA approval processes relating to new drug products differ depending on the nature of the particular product candidate for which approval is sought. With respect to any product candidate with active ingredients not previously approved by the FDA, a prospective drug product manufacturer is required to submit an NDA that includes complete reports of pre-clinical, clinical and laboratory studies and extensive manufacturing information to demonstrate such product s safety and effectiveness. The NDA process generally requires, before the submission of the NDA, filing of an investigational new drug application, or IND, pursuant to which permission is sought to begin clinical testing of the new product candidate. An NDA based on published safety and effectiveness studies conducted by others, or previous findings of safety and effectiveness by the FDA, may be submitted under Section 505(b)(2) of the Federal Food, Drug and Cosmetic Act, or the FDCA.

Generally, with respect to any product candidate with active ingredients not previously approved by the FDA, an NDA must be supported by data from at least phase 1, phase 2 and phase 3 clinical trials. Phase 1 clinical trials can be expected to last from 6 to 18 months, phase 2 clinical trials can be expected to last from 12 to 24 months and phase 3 clinical trials can be expected to last from 18 to 36 months. However, clinical development timelines vary widely, as do the total costs of clinical trials and the likelihood of success. We anticipate that we will make determinations as to which of our R&D programs to pursue and how much funding to direct to each R&D program on an ongoing basis in response to the scientific, nonclinical and clinical success of the underlying product candidate, our ongoing assessment of its market potential and our available resources.

Future expenditures on R&D programs are subject to many uncertainties, including whether we will further develop our product candidates with a partner or independently. At this time, due to such uncertainties and the risks inherent in drug product development and the associated regulatory process, we cannot estimate with reasonable certainty the duration of or costs to complete our R&D programs or whether or when or to what extent revenues will be generated from the commercialization and sale of any of our product candidates. The duration and costs of our R&D programs, in particular those associated with clinical and bioequivalence trials and research-related manufacturing, can vary significantly among programs as a result of a variety of factors, including:

- the number of trials necessary to demonstrate the safety and efficacy of a product candidate;
- the number of patients who participate in the trials;

Table of Contents

- the number and location of sites included in trials and the rate of site approval for the trial;
- the rates of patient recruitment and enrollment;
- the ratio of randomized to evaluable patients;
- the time and cost of process development activities related to our product candidates;
- the costs of manufacturing our product candidates;
- with respect to bioequivalence or comparative trials, the availability and cost of reference or control product in the jurisdiction of each site;
- the duration of patient treatment and follow-up;
- the time and cost of stability studies, including the need to identify critical parameters, methods to evaluate and test these parameters and validation of such methods and tests; and
- the costs, requirements, timing of and the ability to secure regulatory approvals.

The difficult process of seeking regulatory approvals for our product candidates, in particular any containing new chemical entities, and compliance with applicable regulations requires the expenditure of substantial resources. Any failure by us to obtain, or any delay in obtaining, regulatory approvals could cause our R&D expenditures to increase and, in turn, have a material and unfavorable effect on our results of operations. We cannot be certain when, if ever, we will generate revenues from sales of any of our product candidates.

While many of our R&D expenses are transacted in U.S. dollars, certain significant expenses are required to be paid in foreign currencies and expose us to transaction gains and losses that could result from changes in foreign currency exchange rates. In particular, our current contract manufacturer, which is also our intended commercial manufacturer, for both Exelbine and ANX-514 is located outside the U.S. and generally we pay for its services in Euros. As a result, our exposure to currency risk likely will increase as we move our products towards commercialization and increase the services we request from our current contract manufacturer. We include realized gains and losses from foreign currency transactions in operations as incurred.

We operate our business and evaluate our company on the basis of a single reportable segment, which is the business of acquiring, developing and commercializing proprietary product candidates principally for the treatment of cancer. As a development-stage company, we have not generated any revenue from product sales to date, and we do not expect to generate revenue from product sales until such time that we have obtained approval from a regulatory agency to sell one or more of our product candidates, which we cannot predict will occur.

In 2010 and 2009, our R&D expenses consisted primarily of costs associated with nonclinical activities related to Exelbine and ANX-514, including regulatory-related consulting services, research-related manufacturing services and stability testing and a toxicology study of Exelbine. Our most significant R&D expenses were those relating to the submission and resubmission of our Exelbine NDA to the FDA. Our selling, general and administrative, or SG&A, expenses for the same periods consisted primarily of consultants fees for performing finance, accounting, human resources, facilities, internal systems support, business development, commercialization and investor relations functions activities, salaries, benefits and related personnel costs for employees, including our executive officers, and share-based compensation expense. The following table illustrates the types of operating expenses we incurred in 2010 and 2009 and their respective percent of our total operating costs for those periods:

	Operating Expenses Years Ended December 31,	
	2010	**2009**
Research and development	41%	56%
Selling, general and administrative	59%	43%
Depreciation and amortization	0%	1%
Total operating expenses	100%	100%

Table of Contents

Comparison of 2010 and 2009

Revenue. We recognized revenue of $0.5 million for the year ended December 31, 2010 and $0.3 million for the year ended December 31, 2009. Revenue in 2010 consists of two grants awarded under the qualifying therapeutic discovery project established under Section 48D of the Internal Revenue Code as a result of the Patient Protection and Affordable Care Act of 2010 and paid in November 2010. Revenue in 2009 consists of a nonrefundable license fee under our March 2009 license agreement with respect to ANX-514 with Shin Poong Pharmaceutical Co., Ltd.

R&D Expenses. We maintain and evaluate our R&D expenses by the type of cost incurred rather than by project. We maintain and evaluate R&D expenses by type primarily because we outsource a substantial portion of our work and our R&D personnel and consultants work across multiple programs rather than dedicating their time to one particular program. We began maintaining such expenses by type on January 1, 2005. The following table summarizes our consolidated R&D expenses by type for each of the periods listed:

	Years Ended December 31,		January 1, 2005 through December 31,
	2010	2009	2010
External bioequivalence and clinical trial fees and expenses	$ 215,486	$ 603,097	$ 24,018,062
External nonclinical study fees and expenses (1)	3,225,723	5,083,474	27,254,671
Personnel costs	253,298	779,510	10,543,996
Share-based compensation expense	(5,745)	41,569	2,919,985
Total	$ 3,688,762	$ 6,507,650	$ 64,736,714

(1) External nonclinical study fees and expenses include preclinical, research-related manufacturing, quality assurance and regulatory expenses.

R&D expenses decreased by $2.8 million, or 43%, to $3.7 million for the year ended December 31, 2010, compared to $6.5 million for the year ended December 31, 2009. The decrease in R&D expenses in 2010 compared to 2009 was due primarily to a $1.9 million decrease in external nonclinical study fees and expenses. This decrease resulted largely from a $2.6 million decrease in costs of research-related manufacturing activities for Exelbine and a $0.1 million decrease in fees for regulatory-related consulting services related to Exelbine, partially offset by a $0.5 million increase in fees for regulatory-related consulting services related to ANX-514 and a $0.3 million increase in toxicology study expenses related to Exelbine. The decrease in personnel costs was attributable primarily to lower headcount in 2010 compared to 2009 and completion in 2009 of severance payments associated with our 2009 and 2008 workforce reductions. The decrease in external bioequivalence and clinical trial fees and expenses in 2010 compared to 2009 was due primarily to the release of residual accruals for expenses related to ANX-510 clinical trials that were completed in the fourth quarter of 2008 and the first quarter of 2009. The decrease in share-based compensation expense resulted primarily from the forfeiture of stock option awards in connection with employee terminations in 2009 and 2008.

We expect R&D expenses to be a significantly larger component of our total operating expenses in 2011 compared to 2010. We expect R&D expenses to increase in 2011 relative to 2010 to support continued development of ANX-514, to pursue development of purified 188, should our acquisition of SynthRx close, and to pursue development of any other technologies and/or product candidates we may acquire, including potentially adding new clinical, regulatory and manufacturing personnel.

Selling, General and Administrative Expenses. SG&A expenses were relatively flat year to year, with an increase of $0.3 million, or approximately 6%, to $5.3 million for the year ended December 31, 2010, compared to $5.0 million for the year ended December 31, 2009. In 2010 compared to 2009, fees for third-party services related to commercial-readiness activities related to Exelbine and identifying and evaluating strategic opportunities for our

product candidates and pipeline expansion increased by $0.3 million, consulting fees related to our finance, accounting, human resources, facilities and internal systems support increased by $0.2 million, our Delaware corporate franchise tax increased by $0.2 million and share-based compensation expense increased by $0.2 million. These increases were partially offset by a $0.5 million decrease in personnel costs, primarily as a result of lower headcount and the absence of severance costs in 2010, and a $0.1 million decrease in professional fees for legal, audit and tax services.

Table of Contents

We expect SG&A expenses to increase in 2011 relative to 2010 as we prepare for the commercial launch of Exelbine and, should it be approved, as we launch Exelbine, and any other products we may acquire, including potentially adding sales and marketing personnel, and to support continued development of ANX-514, pursue development of purified 188, should our acquisition of SynthRx close, and pursue development of any other technologies, product candidates and/or we may acquire.

Interest and Other Income/(Expense). Interest income amounted to $93,000 for 2010, compared to $7,000 in 2009. The increase in interest income of $86,000 for 2010 was primarily attributable to overall higher invested balances, though offset partially by lower interest rates earned. Even though we raised a substantial amount of additional capital through our January and May 2010 and January 2011 registered direct equity financings, we expect that interest income will continue to be low due to negligible interest rates. Other expense was $2,000 in 2010, compared to $47,000 in 2009. Both years expense was attributable to losses on the sale of various business assets.

Net Loss. Net loss applicable to common stock was $14.1 million, or $1.07 per share, for the year ended December 31, 2010, compared to a net loss applicable to common stock of $16.2 million, or $3.47 per share, for the year ended December 31, 2009. Included in the net loss applicable to common stock for 2010 and 2009 were non-cash deemed dividend expenses of approximately $5.6 million and $4.9 million, respectively, related to our January and May 2010 and June, July, August and October 2009 registered direct equity financings. Included in both net loss and net loss applicable to common stock for 2009 were charges associated with our 2009 and 2008 workforce reductions.

Liquidity and Capital Resources

We have a history of annual losses from operations and we have funded our operations primarily through sales of our equity securities. We had a net loss of $8.5 million for the year ended December 31, 2010 and cash of approximately $28.0 million as of December 31, 2010.

In January and May 2010, we completed registered direct equity financings involving the issuance, respectively, of units consisting of shares of our Series E Stock and our Series F Stock and common stock purchase warrants. These financings resulted in an aggregate of $38.2 million in gross proceeds, and we received an aggregate of $27.4 million in net proceeds after deducting amounts deposited into escrow accounts to fund our dividend and related payment obligations in respect of the Series E Stock and Series F Stock, the fees and expenses of our placement agent and financial advisor in the financings, and our other offering expenses. As of December 31, 2010, all of the shares of our Series E Stock and Series F Stock had been converted into common stock and are no longer outstanding.

In January 2010, we received an aggregate of $0.3 million of net proceeds and issued an aggregate of 84,651 shares of our common stock in connection with the exercise of warrants issued in our June 2009 registered direct equity financing.

In November 2010, the Internal Revenue Service notified us that an aggregate amount of $488,959 in grants had been awarded to us under the qualifying therapeutic discovery project, or QTDP, program established under Section 48D of the Internal Revenue Code as a result of the Patient Protection and Affordable Care Act of 2010. We submitted applications in July 2010 for qualified investments we made, or expected to make, in 2009 and 2010 in our Exelbine and ANX-514 programs, and a grant in the amount of $244,479 was approved for each of those programs. These grants are not taxable for federal income tax purposes. We received full payment of the grants in November 2010.

In January 2011, we completed a registered direct equity financing involving the issuance of shares of our common stock and common stock purchase warrants. This financing resulted in $22.5 million in gross proceeds, and we received $21.0 million in net proceeds after deducting the fees and expenses of our placement agent and our other offering expenses.

Table of Contents

We may receive up to $0.8 million, $4.4 million, $9.5 million and $11.3 million of additional net proceeds from the exercise of warrants issued in the registered direct equity financings we completed in October 2009, January and May 2010 and January 2011, respectively; however, the exercise of these warrants is subject to certain beneficial ownership limitations. In addition, we may receive up to $3.7 million of additional net proceeds from the exercise of warrants issued to our placement agent as additional consideration for services in connection with certain of our registered direct equity financings.

For a more detailed discussion of our 2009 and 2010 equity financings, see Note 6, Capital Stock and Warrants, of the Notes to Consolidated Financial Statements in this report.

For a discussion of our liquidity and capital resources outlook, see Management Outlook below.

Analysis of our 2010 versus 2009 cash flow from operating, investing and financing activities is provided below.

	December 31, 2010	Increase During 2010	December 31, 2009
Cash	$ 27,978,823	$ 19,311,419	$ 8,667,404
Net working capital	$ 26,607,603	$ 19,988,796	$ 6,618,807

	Year Ended December 31, 2010	Change Between Periods	Year Ended December 31, 2009
Net cash used in operating activities	$ (8,341,237)	$ 4,275,179	$ (12,616,416)
Net cash provided by (used in) investing activities	(24,134)	(40,134)	16,000
Net cash provided by financing activities	27,676,790	16,258,874	11,417,916
Net increase (decrease) in cash	$ 19,311,419	$ 20,493,919	$ (1,182,500)

Operating activities. Net cash used in operating activities was $8.3 million in 2010, compared to $12.6 million in 2009. The decrease in cash used in operating activities in 2010 was due primarily to realization of financial benefit from the restructuring, cost-cutting and re-prioritization initiatives we implemented beginning in October 2008 through June 2009; specifically, our workforce reductions and our discontinuation of active work on all compounds, other than Exelbine and ANX-514, to which we have or had rights during that period.

Investing activities. Net cash used in investing activities was $24,134 in 2010, compared to $16,000 provided by investing activities in 2009. The cash used in investing activities in 2010 was primarily for purchases of property and equipment offset by $4,379 of proceeds from sale of property and equipment. The $16,000 provided by investing activities in 2009 was from proceeds from sale of property and equipment.

Financing activities. Net cash provided by financing activities was $27.7 million in 2010, compared to $11.4 million in 2009. The cash provided by financing activities in 2010 and 2009 primarily consisted of proceeds from the issuance of our equity securities in the financing transactions we completed during those periods.

Management Outlook

We anticipate that our cash as of December 31, 2010, together with the net proceeds from the equity financing we completed in January 2011, will be sufficient to fund our currently planned level of operations for at least the next 12 months. However, our future capital uses and requirements will be affected by numerous forward- looking factors that, depending on their actual outcome, could shorten or extend the period through which our operating funds will sustain us. These factors include, but are not limited to: the extent to which we acquire new technologies, product candidates, products or businesses; the scope, prioritization and number of development and/or commercialization programs we pursue; the rate of progress and costs of development and regulatory approval activities associated with our product candidates, including conducting manufacturing process development activities and manufacturing clinical trial material; the rate of progress and costs to comply with post-approval requirements imposed on our products candidates, should any be approved; the extent to which we partner or collaborate with third parties to develop, seek regulatory approval of and commercialize our product candidates or products, or sell or license our

product candidates or products to others; the costs and timing of acquiring or developing sales, marketing and distribution capabilities and the regulatory compliance and administrative capabilities to commercialize Exelbine in the U.S., regardless of whether Exelbine is ultimately approved by the FDA; the costs and timing of acquiring or developing similar commercialization capabilities for other of our product candidates, including ANX-514, and product candidates or products we may acquire in the future, including purified 188 should our acquisition of SynthRx close; and whether any of our product candidates for which we receive regulatory approval, if any, achieve broad market acceptance. In addition, currently, we have only three full-time employees and one part-time employee and rely on third parties to perform many essential services for us. Increasing the size of our workforce will also impact the period through which our operating funds will sustain us, but the timing and extent to which we do so is difficult to predict as it will be influenced by the rate of progress of development and regulatory approval of our product candidates and whether we partner them, as well as the extent to which we acquire and develop new technologies, product candidates, products or businesses.

Table of Contents

We continue to undertake commercial-readiness activities with respect to Exelbine to prepare for its launch in the U.S., should the FDA approve our Exelbine NDA. In preparing for the potential commercial launch of Exelbine, we expect to develop or acquire internal marketing, distribution and sales capabilities and associated regulatory compliance capabilities, as well as contract with third parties to supplement and enhance our internal capabilities. Such activities may result in a substantial increase in our workforce in 2011. We continue to evaluate the relative benefits of developing or acquiring these capabilities, as well as the use of third parties. Currently, we cannot forecast with any degree of certainty the costs associated with our Exelbine commercial-readiness activities during 2011.

We also continue to develop ANX-514 following our February 2011 meeting with the FDA. We are in the process of developing a protocol for a phase 3 clinical trial of ANX-514 for submission to the FDA. In 2011, we expect to use capital to develop the phase 3 trial protocol, conduct manufacturing process development activities and manufacture clinical trial material that would enable us to initiate a clinical trial of ANX-514 should we reach agreement with the FDA as to the trial protocol. In parallel, we also expect to continue to pursue partnering and other strategic opportunities for ANX-514, including its sale or exclusive license to a third party. However, partnering and other strategic options may not be available on acceptable terms, if at all. As our discussions with the FDA progress, if we determine the anticipated capital requirements associated with continued development of ANX-514 are not financially justifiable, we may determine to discontinue this program. Currently, we cannot forecast with any degree of certainty the costs associated with our continued development of ANX-514 during 2011.

In February 2011, we entered into an agreement and plan of merger to acquire SynthRx, Inc. in exchange for shares of our common stock. We expect to consummate our acquisition of SynthRx in the first half of 2011. As discussed in more detail under Item 1 Business above, we initially intend to develop purified 188 for the treatment of sickle cell crisis in a pediatric population. If our acquisition of SynthRx closes, we intend to meet with the FDA to reach agreement on a protocol for a phase 3 clinical trial of purified 188 for this indication. In parallel, we expect to prepare to initiate the clinical trial, including conducting manufacturing process development activities and manufacturing clinical material, which could enable us to initiate it in 2012. We also expect to increase our workforce in connection with our acquisition of SynthRx. Until we reach agreement with the FDA on a phase 3 trial protocol, we cannot forecast with any degree of certainty the costs that would be associated with our development of purified 188 for the treatment of sickle cell crisis in a pediatric population. However, our preliminary estimate of third party costs related to this development program through submission of an NDA is approximately $15 million to $25 million.

In addition, in connection with the consummation of the SynthRx acquisition, we would issue 2,938,773 shares of our common stock to SynthRx s stakeholders, 1,938,773 of which would be subject to repurchase by us in the event purified 188 does not achieve the First Milestone. We could issue up to an aggregate of 13,478,050 additional shares of our common stock to SynthRx s stakeholders if the development of purified 188 achieves the First, Second and Third Milestones and our stockholders approve the issuance of such milestone-related shares, as required by NYSE Amex rules. If our stockholders do not approve the issuance of the milestone-related shares, under the terms of the merger agreement, we would be required to pay SynthRx s stakeholders in cash the value of the milestone-related shares we would have otherwise issued, with all such cash payments made in quarterly installments and, with respect to the cash value associated with the Second and Third Milestone shares (an aggregate of 12,478,050 shares), payable based on net sales of purified 188. We cannot determine the amount of our potential cash payments to SynthRx s stakeholders because the amount of such payments, if any, will depend on the 10-day volume weighted average of the closing price of our common stock at the time a milestone is achieved and the market price of our common stock historically has been, and likely will continue to be, highly volatile.

Table of Contents

We continue to spend significant time and attention identifying and evaluating additional opportunities to expand our product pipeline and may do so through one or more in-license, asset acquisition or merger transactions. We continue to believe that, due to a challenging capital raising environment, many drug development programs with substantial potential currently are available at attractive valuations. If we seek to expand our product pipeline through a merger or other business combination with one of these companies, given our recent market capitalization and our desire to preserve our cash for development activities, such a transaction may result in our stockholders owning less than a majority of the voting securities of the surviving entity. The process of identifying and evaluating various opportunities may be lengthy and complex and divert management s attention from our current development programs, and we may not be able to acquire or acquire rights to additional technologies, product candidates and/or products on acceptable terms, or at all. We have limited resources to identify, evaluate and negotiate the acquisition of new technologies, product candidates and/or products or rights thereto and to integrate them into our current infrastructure. Supplementing our current resources to complete one or more transactions may be costly. We anticipate that our capital requirements will increase in future periods if we are successful in expanding our product pipeline.

We may also seek or need to raise additional capital through public or private sales of our equity securities or debt financings. However, we may not be able to obtain additional financing on a timely basis or on acceptable terms, if at all.

Recent Accounting Pronouncements

See Note 2, Summary of Significant Accounting Policies Recent Accounting Pronouncements, of the Notes to Consolidated Financial Statements in this report for a discussion of recent accounting pronouncements and their effect, if any, on us.

Item 7A. Quantitative and Qualitative Disclosures About Market Risk.

Under SEC rules and regulations, as a smaller reporting company we are not required to provide the information required by this item.

Item 8. Financial Statements and Supplementary Data.

The consolidated financial statements and supplementary financial information required by this item are filed with this report as described under Item 15.

Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure.

None.

Item 9A. Controls and Procedures.

Disclosure Controls and Procedures

We maintain disclosure controls and procedures that are designed to ensure that information required to be disclosed by us in the reports we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC s rules and forms, and that such information is accumulated and communicated to our management, including our principal executive officer and principal financial officer, as appropriate to allow timely decisions regarding required disclosure. In designing and evaluating the disclosure controls and procedures, management recognized that any controls and procedures, no matter how well designed and operated, can only provide reasonable assurance of achieving the desired control objectives, and in reaching a reasonable level of assurance, management necessarily was required to apply its judgment in evaluating the cost-benefit relationship of possible controls and procedures.

Table of Contents

Under the supervision and with the participation of our management, including our principal executive officer and principal financial officer, we have evaluated the effectiveness of our disclosure controls and procedures (as defined under Exchange Act Rule 13a-15(e)) as of December 31, 2010. Based on that evaluation, our principal executive officer and principal financial officer have concluded that these disclosure controls and procedures were effective as of December 31, 2010.

Changes in Internal Control over Financial Reporting

There was no change in our internal control over financial reporting identified in connection with the evaluation required by Exchange Act Rules 13a-15(d) and 15d-15(d) that occurred during the fiscal quarter ended December 31, 2010 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

Management s Report on Internal Control over Financial Reporting

Our management is responsible for establishing and maintaining adequate internal control over financial reporting, as such term is defined in Exchange Act Rule 13a-15(f). Under the supervision and with the participation of our management, including our principal executive officer and principal financial officer, we conducted an evaluation of the effectiveness of our internal control over financial reporting based on the framework in *Internal Control Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on our evaluation under the framework in *Internal Control Integrated Framework*, our management concluded that our internal control over financial reporting was effective as of December 31, 2010.

This annual report does not include an attestation report of our independent registered public accounting firm regarding our internal control over financial reporting. Management s report on internal control over financial reporting was not subject to attestation by our independent registered public accounting firm pursuant to the rules of the SEC because we are neither an accelerated filer nor a larger accelerated filer.

Item 9B. Other Information.

Not applicable.

Table of Contents

PART III

Certain information required by Part III is omitted from this report pursuant to General Instruction G(3) of Form 10-K because we will file a definitive proxy statement (the Proxy Statement) within 120 days after the end of our fiscal year pursuant to Regulation 14A for our 2011 annual meeting of stockholders, and such information included in the Proxy Statement is incorporated herein by reference.

Item 10. Directors, Executive Officers and Corporate Governance.

Code of Ethics

We have adopted a code of ethics that applies to our principal executive officer, principal financial officer, principal accounting officer or persons performing similar functions, as well as all of our other officers, directors and employees. This code of ethics is a part of our code of business conduct and ethics, and is available on our corporate website at www.adventrx.com. We intend to disclose future amendments to, or waivers of, certain provisions of our code of ethics that apply to our principal executive officer, principal financial officer, principal accounting officer or persons performing similar functions on the above website within four business days following such amendment or waiver.

The other information required by this item will be set forth in the Proxy Statement and is incorporated into this report by reference.

Item 11. Executive Compensation.

The information required by this item will be set forth in the Proxy Statement and is incorporated into this report by reference.

Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters.

The information required by this item will be set forth in the Proxy Statement and is incorporated into this report by reference.

Item 13. Certain Relationships and Related Transactions, and Director Independence.

The information required by this item will be set forth in the Proxy Statement and is incorporated into this report by reference.

Item 14. Principal Accounting Fees and Services.

The information required by this item will be set forth in the Proxy Statement and is incorporated into this report by reference.

PART IV

Item 15. Exhibits, Financial Statement Schedules.

(a) Documents Filed. The following documents are filed as part of this report:

(1) Financial Statements. The following report of J.H. Cohn LLP and financial statements:

Report of J.H. Cohn LLP, Independent Registered Public Accounting Firm
Consolidated Balance Sheets as of December 31, 2010 and 2009
Consolidated Statements of Operations for the years ended December 31, 2010 and 2009 and from inception through December 31, 2010

Table of Contents

Consolidated Statements of Stockholders Equity (Deficit) and Comprehensive Loss from inception through December 31, 2010
Consolidated Statements of Cash Flows for the years ended December 31, 2010 and 2009 and from inception through December 31, 2010
Notes to Consolidated Financial Statements

(2) Financial Statement Schedules. See subsection (c) below.
(3) Exhibits. See subsection (b) below.

(b) Exhibits.

Exhibit	Description
2.1(1)	Agreement and Plan of Merger, dated April 7, 2006, among the registrant, Speed Acquisition, Inc., SD Pharmaceuticals, Inc. and certain individuals named therein (including exhibits thereto)
3.1(2)	Amended and Restated Certificate of Incorporation of the registrant
3.2(3)	Certificate of Amendment to the Amended and Restated Certificate of Incorporation of the registrant dated October 5, 2009
3.3(4)	Certificate of Amendment to the Amended and Restated Certificate of Incorporation of the registrant, dated April 23, 2010
3.4(5)	Certificate of Designation of Preferences, Rights and Limitations of 0% Series A Convertible Preferred Stock
3.5(6)	Certificate of Designation of Preferences, Rights and Limitations of 5% Series B Convertible Preferred Stock
3.6(7)	Certificate of Designation of Preferences, Rights and Limitations of 5% Series C Convertible Preferred Stock
3.7(8)	Certificate of Designation of Preferences, Rights and Limitations of 4.25660% Series D Convertible Preferred Stock
3.8(9)	Certificate of Designation of Preferences, Rights and Limitations of 3.73344597664961% Series E Convertible Preferred Stock
3.9(10)	Certificate of Designation of Preferences, Rights and Limitations of 2.19446320054018% Series F Convertible Preferred Stock
3.10(11)	Amended and Restated Bylaws of the registrant (formerly known as Biokeys Pharmaceuticals, Inc.)
10.1(12)	Securities Purchase Agreement, dated July 21, 2005, among the registrant and the Purchasers (as defined therein)
10.2(12)	Rights Agreement, dated July 27, 2005, among the registrant, the Icahn Purchasers and Viking (each as defined therein)

10.3(13)	First Amendment to Rights Agreement, dated September 22, 2006, among the registrant and the Icahn Purchasers (as defined therein)
10.4(14)	Second Amendment to Rights Agreement, dated February 25, 2008, among the registrant and the Icahn Purchasers (as defined therein)
10.5(15)	Third Amendment to Rights Agreement, dated August 26, 2009, among the registrant and Icahn Purchasers (as defined therein)
10.6(12)	Form of $2.26 Common Stock Warrant issued on July 27, 2005 to Icahn Partners LP, Icahn Partners Master Fund LP, High River Limited Partnership, Viking Global Equities LP and VGE III Portfolio Ltd.

Table of Contents

Exhibit	Description
10.7(12)	Form of $2.26 Common Stock Warrant issued on July 27, 2005 to North Sound Legacy Institutional Fund LLC and North Sound Legacy International Ltd.
10.8(5)	Engagement Letter Agreement, dated June 7, 2009, by and between the registrant and Rodman & Renshaw, LLC
10.9(5)	Securities Purchase Agreement, date June 8, 2009, governing the issuance and sale of the registrant s 0% Series A Convertible Preferred Stock and 5-year common stock purchase warrants
10.10(5)	Form of Common Stock Purchase Warrant issued on June 12, 2009 by the registrant to the purchasers of the registrant s 0% Series A Convertible Preferred Stock and to Rodman & Renshaw, LLC
10.11(6)	Engagement Letter Agreement, dated June 26, 2009, by and between the registrant and Rodman & Renshaw, LLC
10.12(6)	Securities Purchase Agreement, dated June 29, 2009, governing the issuance and sale of the registrant s 5% Series B Convertible Preferred Stock
10.13(6)	Form of Common Stock Purchase Warrant issued on July 6, 2009 by the registrant to Rodman & Renshaw, LLC
10.14(7)	Engagement Letter Agreement, dated August 4, 2009, by and between the registrant and Rodman & Renshaw, LLC
10.15(7)	Securities Purchase Agreement, dated August 5, 2009, governing the issuance and sale of the registrant s 5% Series C Convertible Preferred Stock
10.16(7)	Form of Common Stock Purchase Warrant issued on August 10, 2009 by the registrant to Rodman & Renshaw, LLC
10.17(16)	Engagement Letter Agreement, dated September 24, 2009, by and between the registrant and Rodman & Renshaw, LLC
10.18(8)	Engagement Letter Agreement, dated September 29, 2009, by and between the registrant and Rodman & Renshaw, LLC
10.19(8)	Form of Securities Purchase Agreement, dated October 6, 2009, governing the issuance and sale of the registrant s 4.25660% Series D Convertible Preferred Stock and 5-year common stock purchase warrants
10.20(8)	Form of Common Stock Purchase Warrant issued on October 9, 2009 by the registrant to the purchasers of the registrant s 4.25660% Series D Convertible Preferred Stock and to Rodman & Renshaw, LLC
10.21(9)	

	Engagement Letter Agreement, dated January 3, 2010, by and between the registrant and Rodman & Renshaw, LLC
10.22(9)	Securities Purchase Agreement, dated as of January 4, 2010, governing the issuance and sale of the registrant s 3.73344597664961% Series E Convertible Preferred Stock and 30-month common stock purchase warrants
10.23(9)	Form of Common Stock Purchase Warrant issued on January 7, 2010 by the registrant to the purchasers of the registrant s 3.73344597664961% Series E Convertible Preferred Stock and to Rodman & Renshaw, LLC
10.24(10)	Engagement Letter Agreement, dated April 29, 2010, by and between the registrant and Rodman & Renshaw, LLC

Table of Contents

Exhibit	Description
10.25(10)	Form of Securities Purchase Agreement, dated May 2, 2010 governing the issuance and sale of the registrant s 2.19446320054018% Series F Convertible Preferred Stock and 5-year and 1-year common stock purchase warrants
10.26(10)	Form of Series A and B Common Stock Purchase Warrants issued on May 6, 2010 by the registrant to the purchasers of the registrant s 2.19446320054018% Series F Convertible Preferred Stock
10.27(17)	Engagement Letter Agreement, dated January 5, 2011, by and between the registrant and Rodman & Renshaw, LLC
10.28(17)	Form of Securities Purchase Agreement, dated January 6, 2011 governing the issuance and sale of the registrant s common stock and 5-year and 1-year common stock purchase warrants
10.29(17)	Form of [Series A/B] Common Stock Purchase Warrant issued on January 11, 2011 by the registrant to the purchasers of the registrant s common stock and to Rodman & Renshaw, LLC
10.30#(18)	2005 Equity Incentive Plan
10.31#(19)	Form of Stock Option Agreement under the 2005 Equity Incentive Plan
10.32#(20)	Form of Stock Option Agreement under the 2005 Equity Incentive Plan (for director option grants beginning in 2008)
10.33#(21)	Form of Stock Option Agreement under the 2005 Equity Incentive Plan (for option grants to employees approved in March 2008)
10.34#(2)	Form of Restricted Share Award Agreement under the 2005 Equity Incentive Plan
10.35#(22)	2008 Omnibus Incentive Plan
10.36#(23)	Form of Notice of Grant of Restricted Stock Units under the 2008 Omnibus Incentive Plan (for grants to employees in January 2009)
10.37#(23)	Form of Restricted Stock Units Agreement under the 2008 Omnibus Incentive Plan
10.38#(24)	Form of Non-Statutory Stock Option Grant Agreement (for directors) under the 2008 Omnibus Incentive Plan
10.39#(24)	Form of Non-Statutory/Incentive Stock Option Grant Agreement (for consultants/employees) under the 2008 Omnibus Incentive Plan
10.40#(25)	Form of Incentive Stock Option Grant Agreement under the 2008 Omnibus Incentive Plan (for grant to Brian M. Culley in July 2009)
10.41#(25)	

	Form of Incentive Stock Option Grant Agreement under the 2008 Omnibus Incentive Plan (for grant to Patrick L. Keran in July 2009)
10.42#(26)	Form of letter, dated January 20, 2010, modifying options granted to Brian M. Culley and Patrick L. Keran in July 2009
10.43#(26)	Form of Incentive Stock Option Grant Agreement under the 2008 Omnibus Incentive Plan (for grant to Brian M. Culley in January 2010)
10.44#(26)	Form of Incentive Stock Option Grant Agreement under the 2008 Omnibus Incentive Plan (for grant to Patrick L. Keran in January 2010)
10.45(20)	License Agreement, dated December 10, 2005, among SD Pharmaceuticals, Latitude Pharmaceuticals and Andrew Chen, including a certain letter, dated November 20, 2007, clarifying the scope of rights thereunder
10.46 (27)	License Agreement, dated March 25, 2009, among the registrant, SD Pharmaceuticals, Inc. and Shin Poong Pharmaceutical Co., Ltd.
10.47(28)	Standard Multi-Tenant Office Lease Gross, dated June 3, 2004, between the registrant and George V. Casey & Ellen M. Casey, Trustees of the Casey Family Trust dated June 22, 1998

Table of Contents

Exhibit	Description
10.48(2)	First Amendment to the Standard Multi-Tenant Office Lease Gross, dated June 3, 2004 between the registrant and George V. & Ellen M. Casey, Trustees of the Casey Family Trust dated June 22, 1998
10.49(29)	Second Amendment to Standard Mutli-Tenant Office Lease Gross, dated July 22, 2009, by and among Westcore Mesa View, LLC, DD Mesa View LLC and the registrant
10.50(30)	Third Amendment to Standard Multi-Tenant Office Lease Gross, dated December 10, 2009, by and among Westcore Mesa View, LLC, DD Mesa View, LLC and the registrant
10.51(31)	Fourth Amendment to Standard Multi-Tenant Office Lease Gross, dated February 4, 2010, by and among Westcore Mesa View, LLC, DD Mesa View, LLC and the registrant
10.52#(32)	Offer letter, dated November 15, 2004, to Brian M. Culley
10.53#(23)	Retention and Incentive Agreement, dated January 28, 2009 between the registrant and Brian M. Culley
10.54#(27)	Retention and Incentive Agreement, dated January 28, 2009, between the registrant and Patrick L. Keran
10.55#(31)	Consulting Agreement, effective as of July 15, 2009, and Amendment to Consulting Agreement, effective as of December 31, 2009, between the registrant and Michele L. Yelmene
10.56#(25)	2009 Mid-Year Incentive Plan for Brian M. Culley and Patrick L. Keran
10.57#(25)	Retention and Severance Plan (as of July 21, 2009) for Brian M. Culley and Patrick L. Keran
10.58#(26)	2010 Incentive Plan for Brian M. Culley and Patrick L. Keran
10.59#(31)	Consulting Agreement, effective as of November 23, 2009, between the registrant and Eric K. Rowinsky
10.60#(33)	Director Compensation Policy, adopted June 21, 2006
10.61#(31)	Director Compensation Policy, adopted January 25, 2010
10.62(34)	Form of Director and Officer Indemnification Agreement
21.1	List of Subsidiaries
23.1	Consent of J.H. Cohn LLP, Independent Registered Public Accounting Firm
31.1	Certification of principal executive officer pursuant to Rule 13a-14(a)/15d-14(a)
31.2	Certification of principal financial officer pursuant to Rule 13a-14(a)/15d-14(a)

32.1±	Certification of principal executive officer and principal financial officer pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

Indicates that confidential treatment has been requested or granted to certain portions, which portions have been omitted and filed separately with the SEC

# Indicates management contract or compensatory plan

± These certifications are being furnished solely to accompany this report pursuant to 18 U.S.C. 1350, and are not being filed for purposes of Section 18 of the Securities Exchange Act of 1934 and are not to be incorporated by reference into any filing of the registrant, whether made before or after the date hereof, regardless of any general incorporation by reference language in such filing.

(1) Filed with the registrant s Amendment No. 1 to Current Report on Form 8-K/A on May 1, 2006 (SEC file number 001-32157-06796248)

Table of Contents

(2) Filed with the registrant s Annual Report on Form 10-K on March 16, 2006 (SEC file number 001-32157-06693266)

(3) Filed with the registrant s Current Report on Form 8-K on October 13, 2009 (SEC file number 001-32157-091115090)

(4) Filed with the registrant s Current Report on Form 8-K on April 26, 2010 (SEC file number 001-32157-10769058)

(5) Filed with the registrant s Current Report on Form 8-K on June 8, 2009 (SEC file number 001-32157-09878961)

(6) Filed with the registrant s Current Report on Form 8-K on June 30, 2009 (SEC file number 001-32157-09917820)

(7) Filed with the registrant s Current Report on Form 8-K on August 5, 2009 (SEC file number 001-32157-09989205)

(8) Filed with the registrant s Amendment No. 3 to the Registration Statement on Form S-1 on October 5, 2009 (SEC file number 333-160778-091107945)

(9) Filed with the registrant s Current Report on Form 8-K on January 4, 2010 (SEC file number 001-32157-10500379)

(10) Filed with the registrant s Current Report on Form 8-K on May 3, 2010 (SEC file number 001-32157-10790486)

(11) Filed with the registrant s Current Report on Form 8-K on December 15, 2008 (SEC file number 001-32157-081249921)

(12) Filed with the registrant s Quarterly Report on Form 10-Q on August 12, 2005 (SEC file number 001-32157-051022046)

(13) Filed with the registrant s Current Report on Form 8-K on September 22, 2006 (SEC file number 001-32157-061103268)

(14) Filed with the registrant s Current Report on Form 8-K on February 25, 2008 (SEC file number 001-32157 08638638)

(15) Filed with the registrant s Current Report on Form 8-K on September 1, 2009 (SEC file number 001-32157-091049161)

(16) Filed with the registrant s Amendment No. 2 to the Registration Statement on Form S-1 on September 25, 2009 (SEC file number 333-160778-091087750)

(17) Filed with the registrant s Current Report on Form 8-K on January 7, 2011 (SEC file number 001-32157-11515655)

(18) Filed with the registrant s Annual Report on Form 10-K on March 15, 2007 (SEC file number 001-32157-07697283)

(19) Filed with the registrant s Registration Statement on Form S-8 on July 13, 2005 (SEC file number 333-126551-05951362)

(20) Filed with registrant s Annual Report on Form 10-K on March 17, 2008 (SEC file number 001-32157-08690952)

(21) Filed with the registrant s Quarterly Report on Form 10-Q on May 12, 2008 (SEC file number 001-32157-08820541)

(22) Filed with the registrant s Current Report on Form 8-K on June 2, 2008 (SEC file number 001-32157-08874724)

(23) Filed with the registrant s Current Report on Form 8-K on February 2, 2009 (SEC file number 001-32157-09561715)

(24) Filed with the registrant s Quarterly Report on Form 10-Q on August 11, 2008 (SEC file number 001-32157-081005744)

Table of Contents

(25) Filed with the registrant s Current Report on Form 8-K on July 22, 2009 (SEC file number 001-32157-09957353)

(26) Filed with the registrant s Current Report on Form 8-K on January 26, 2010 (SEC file number 001-32157-10547818)

(27) Filed with the registrant s Quarterly Report on Form 10-Q on May 15, 2009 (SEC file number 001-32157-09878961)

(28) Filed with the registrant s Quarterly Report on Form 10-QSB on August 10, 2004 (SEC file number 001-32157-04963741)

(29) Filed with the registrant s Current Report on Form 8-K on August 20, 2009 (SEC file number 001-32157-091025631)

(30) Filed with the registrant s Current Report on Form 8-K on December 24, 2009 (SEC file number 001-32157-091260100)

(31) Filed with the registrant s Annual Report on Form 10-K on March 18, 2010 (SEC file number 001-32157-10692317)

(32) Filed with the registrant s Annual Report on Form 10-KSB on March 31, 2005 (SEC file number 001-32157-05719975)

(33) Filed with the registrant s Current Report on Form 8-K on June 23, 2006 (SEC file number 001-32157-06922676)

(34) Filed with the registrant s Current Report on Form 8-K on October 23, 2006 (SEC file number 001-32157-061156993)

(c) Financial Statement Schedules. All schedules are omitted because they are not applicable, the amounts involved are not significant or the required information is shown in the financial statements or notes thereto.

Table of Contents

SIGNATURES

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

Date: March 10, 2011

ADVENTRX Pharmaceuticals, Inc.

By: /s/ Brian M. Culley
Brian M. Culley
Chief Executive Officer

KNOW ALL PERSONS BY THESE PRESENTS, that each person whose signature appears below constitutes and appoints Brian M. Culley and Patrick L. Keran, and each of them acting individually, as his true and lawful attorneys-in-fact and agents, each with full power to act alone, with full powers of substitution and resubstitution, for him and in his name, place and stead, in any and all capacities, to sign any and all amendments to this annual report on Form 10-K, and to file the same, with all exhibits thereto and other documents in connection therewith, with the Securities and Exchange Commission, granting unto said attorneys-in-fact and agents full power and authority to do and perform each and every act and thing requisite and necessary to be done in connection therewith, as fully for all intents and purposes as he might or could do in person, hereby ratifying and confirming all that said attorneys-in-fact and agents, or any of them or their substitute or resubstitute, may lawfully do or cause to be done by virtue hereof.
Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

Signature	Title	Date
/s/ Brian M. Culley Brian M. Culley	Chief Executive Officer (Principal Executive Officer)	March 10, 2011
/s/ Patrick L. Keran Patrick L. Keran	President and Chief Operating Officer (Principal Financial and Accounting Officer)	March 10, 2011
/s/ Jack Lief Jack Lief	Chair of the Board	March 10, 2011
/s/ Michael M. Goldberg Michael M. Goldberg	Director	March 10, 2011
/s/ Odysseas D. Kostas Odysseas D. Kostas	Director	March 10, 2011
/s/ Mark J. Pykett Mark J. Pykett	Director	March 10, 2011
/s/ Eric K. Rowinsky	Director	March 10, 2011

Eric K. Rowinsky

Table of Contents

Index to Consolidated Financial Statements

Financial statement schedules have been omitted for the reason that the required information is presented in financial statements or notes thereto, the amounts involved are not significant or the schedules are not applicable.

Table of Contents

Report of Independent Registered Public Accounting Firm

To the Board of Directors and Stockholders
ADVENTRX Pharmaceuticals, Inc.

We have audited the accompanying consolidated balance sheets of ADVENTRX Pharmaceuticals, Inc. and Subsidiaries (a development stage enterprise) as of December 31, 2010 and 2009, and the related consolidated statements of operations, stockholders equity (deficit) and comprehensive loss and cash flows for the years then ended and for the period from January 1, 2002 through December 31, 2010. These consolidated financial statements are the responsibility of the Company s management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, such consolidated financial statements present fairly, in all material respects, the financial position of ADVENTRX Pharmaceuticals, Inc. and Subsidiaries (a development stage enterprise) as of December 31, 2010 and 2009, and their results of operations and cash flows for years then ended and for the period from January 1, 2002 through December 31, 2010, in conformity with accounting principles generally accepted in the United States of America.

/s/ J. H. COHN LLP
San Diego, California
March 10, 2011

Table of Contents

ADVENTRX Pharmaceuticals, Inc. and Subsidiaries
(A Development Stage Enterprise)
Consolidated Balance Sheets

	December 31, 2010	December 31, 2009
Assets		
Current assets:		
Cash	$ 27,978,823	$ 8,667,404
Interest and other receivables	1,980	14,841
Prepaid expenses	428,276	290,249
Total current assets	28,409,079	8,972,494
Property and equipment, net	44,254	44,210
Other assets	33,484	10,513
Total assets	$ 28,486,817	$ 9,027,217
Liabilities and Stockholders Equity		
Current liabilities:		
Accounts payable	$ 479,780	$ 385,358
Accrued liabilities	864,857	1,379,010
Accrued compensation and payroll taxes	456,839	589,319
Total current liabilities	1,801,476	2,353,687
Commitments and contingencies		
Stockholders equity:		
Convertible Preferred Stock, Series A through F, $0.001 par value; 53,776.13 and 15,559 shares authorized as of December 31, 2010 and 2009, respectively; 0 shares issued and outstanding at December 31, 2010 and 2009		
Common stock, $0.001 par value; 500,000,000 shares authorized; 15,480,302 and 8,211,410 shares issued and outstanding at December 31, 2010 and 2009, respectively	15,480	8,211
Additional paid-in capital	182,798,982	148,703,722
Deficit accumulated during the development stage	(156,129,121)	(142,038,403)
Total stockholders equity	26,685,341	6,673,530
Total liabilities and stockholders equity	$ 28,486,817	$ 9,027,217

See accompanying notes to consolidated financial statements.

Table of Contents

ADVENTRX Pharmaceuticals, Inc. and Subsidiaries
(A Development Stage Enterprise)
Consolidated Statements of Operations

	Years Ended December 31,		Inception (June 12, 1996) Through December 31,
	2010	2009	2010
Licensing revenue	$	$ 300,000	$ 1,300,000
Net sales			174,830
Grant revenue	488,959		618,692
Total net revenue	488,959	300,000	2,093,522
Cost of sales			51,094
Gross margin	488,959	300,000	2,042,428
Operating expenses:			
Research and development	3,688,762	6,507,650	72,210,967
Selling, general and administrative	5,320,073	4,998,307	53,287,583
Depreciation and amortization	19,821	79,728	10,897,618
In-process research and development			10,422,130
Impairment loss write-off of goodwill			5,702,130
Equity in loss of investee			178,936
Total operating expenses	9,028,656	11,585,685	152,699,364
Loss from operations	(8,539,697)	(11,285,685)	(150,656,936)
Loss on fair value of warrants			(12,239,688)
Interest income	92,873	7,162	4,682,061
Interest expense	(1,629)		(180,719)
Other income (expense)	(2,469)	(46,535)	63,375
Loss before income taxes	(8,450,922)	(11,325,058)	(158,331,907)
Provision for income taxes			
Loss before cumulative effect of change in accounting principle	(8,450,922)	(11,325,058)	(158,331,907)
Cumulative effect of change in accounting principle			(25,821)
Net loss	(8,450,922)	(11,325,058)	(158,357,728)

Preferred stock dividends			(621,240)
Deemed dividends on preferred stock	(5,639,796)	(4,866,887)	(10,506,683)
Net loss applicable to common stock	$ (14,090,718)	$ (16,191,945)	$ (169,485,651)
Loss per common share basic and diluted	$ (1.07)	$ (3.47)	
Weighted average shares outstanding basic and diluted	13,180,583	4,667,160	

See accompanying notes to consolidated financial statements.

Table of Contents

ADVENTRX Pharmaceuticals, Inc. and Subsidiaries
(A Development Stage Enterprise)
Consolidated Statements of Stockholders Equity (Deficit) and Comprehensive Loss
Inception (June 12, 1996) Through December 31, 2010

	Cumulative convertible preferred stock, series A through C		Convertible preferred stock, series A (2009)		Cumulative convertible preferred stock, series B through F (2009 - 2010)		Common stock		Additional paid-in capital	Accumulated other comprehensive income (loss)	Deficit accumulated during the development stage	Treasury stock, at cost	Total stockholders equity (deficit)	Comprehensive loss
	Shares	Amount	Shares	Amount	Shares	Amount	Shares	Amount						
Balances at June 12, 1996 (date of incorporation)		$		$		$		$		$	$	$	$	
Sale of common stock without par value							20		10				10	
Issuance of common stock and net liabilities assumed in acquisition							68,645	69	4,871		(18,094)		(13,154)	
Issuance of common stock							80,405	80	2,386		(2,466)			
Net loss											(259,476)		(259,476)	$ (259,476)
Balances at December 31, 1996							149,070	149	7,267		(280,036)		(272,620)	$ (259,476)
Sale of common stock, net of offering costs of $9,976							40,182	40	1,790,939				1,790,979	

Issuance of common stock in acquisition	15,036	15	888,235		888,250	
Minority interest deficiency at acquisition charged to the Company				(45,003)	(45,003)	
Net loss				(1,979,400)	(1,979,400)	$ (1,979,400)
Balances at December 31, 1997	204,288	204	2,686,441	(2,304,439)	382,206	$ (1,979,400)
Rescission of acquisition	(15,036)	(15)	(888,235)	561,166	(327,084)	
Issuance of common stock at conversion of notes payable	18,011	18	363,982		364,000	
Expense related to stock warrants issued			260,000		260,000	
Net loss				(1,204,380)	(1,204,380)	$ (1,204,380)
Balances at December 31, 1998	207,263	207	2,422,188	(2,947,653)	(525,258)	$ (1,204,380)
Sale of common stock	27,136	27	134,973		135,000	
Expense related to stock warrants issued			212,000		212,000	
Net loss				(1,055,485)	(1,055,485)	$ (1,055,485)
Balances at December 31, 1999	234,399	234	2,769,161	(4,003,138)	(1,233,743)	$ (1,055,485)

Sale of preferred stock, net of offering costs of $76,500	3,200	32			3,123,468		3,123,500	
Issuance of common stock at conversion of notes and interest payable			16,499	16	492,481		492,497	
Issuance of common stock at conversion of notes payable			2,814	3	83,997		84,000	
Issuance of common stock to settle obligations			19,804	20	1,202,140		1,202,160	
Issuance of common stock for acquisition			280,000	280	9,332,489		9,332,769	
Issuance of warrants for acquisition					4,767,664		4,767,664	
Stock issued for acquisition costs			6,000	6	487,494		487,500	
Expense related to stock warrants issued					140,000		140,000	
Dividends payable on preferred stock					(85,000)		(85,000)	
Cashless exercise of warrants			23,963	24	(24)			
Net loss						(3,701,084)	(3,701,084)	$ (3,701,084)
Balances at December 31, 2000	3,200	32	583,479	583	22,313,870	(7,704,222)	14,610,263	$ (3,701,084)

See accompanying notes to consolidated financial statements.

Table of Contents

ADVENTRX Pharmaceuticals, Inc. and Subsidiaries
(A Development Stage Enterprise)
Consolidated Statements of Stockholders Equity (Deficit) and Comprehensive Loss
Inception (June 12, 1996) Through December 31, 2010

	Cumulative convertible preferred stock, series A through C		Convertible preferred stock, series A (2009)		Cumulative convertible preferred stock, series B through F (2009 - 2010)		Common stock		Additional paid-in capital	Accumulated other comprehensive income (loss)	Deficit accumulated during the development stage	Treasury stock, at cost	Total stockholders equity (deficit)	Comprehensive loss
	Shares	Amount	Shares	Amount	Shares	Amount	Shares	Amount						
vidends yable on ferred ck		$		$		$		$	$ (256,000)	$	$	$	$ (256,000)	
purchase of rrants									(55,279)				(55,279)	
e of rrants									47,741				47,741	
shless ercise of rrants							8,740	9	(9)					
uance of mmon stock pay ferred idends							3,737	4	212,996				213,000	
tachable rrants ued with es payable									450,000				450,000	
uance of rrants to operating penses									167,138				167,138	
uance of mmon stock pay erating penses							4,252	4	387,267				387,271	

uance of ferred ck to pay erating penses	137	1			136,499		136,500	
t loss						(16,339,120)	(16,339,120)	$ (16,339,1
lances at cember 31, 01	3,337	33	600,208	600	23,404,223	(24,043,342)	(638,486)	$ (16,339,1
vidends vable on ferred ck					(242,400)		(242,400)	
purchase of rrants								
e of rrants			9,600	10	117,843		117,853	
shless ercise of rrants			4,008	4	(4)			
ercise of rrants			13,783	14	168,808		168,822	
e of ferred ck at $1.50 share	200,000	2,000			298,000		300,000	
e of ferred ck at .00 per re	70,109	701			700,392		701,093	
nversion of ferred ck into mmon stock	(3,000)	(30)	72,000	72	(42)			
ferred ck idends given					335,440		335,440	
uance of rrants to operating penses					163,109		163,109	
uance of mmon stock pay erating			251		12,269		12,269	

penses uance of ferred ck to pay erating								
penses	136	1			6,000		6,001	
uance of ck options employees					329,296		329,296	
t loss						(2,105,727)	(2,105,727)	$ (2,105,7
ances at cember 31, 02	270,582	2,705	699,850	700	25,292,934	(26,149,069)	(852,730)	$ (2,105,7
vidends vable on ferred ck					(37,840)		(37,840)	
nversion of ies C ferred ck into mmon stock	(70,109)	(701)	560,874	561	140			
uance of mmon stock pay interest Bridge tes			6,633	7	53,484		53,491	
e of mmon stock 0.40 per re, net of uance costs			265,630	266	2,597,066		2,597,332	
e of mmon stock 1.00 per re, net of uance costs			148,069	148	3,992,701		3,992,849	
change of rrants			9,412	9	49,712		49,721	
uance of mmon stock pay erating								
penses			9,200	9	206,790		206,799	
uance of rrants to operating					156,735		156,735	

penses									
uance of									
ck options									
employees					286,033		286,033		
t loss						(2,332,077)	(2,332,077)	$	(2,332,0
lances at									
cember 31,									
03	200,473	2,004	1,699,668	1,700	32,597,755	(28,481,146)	4,120,313	$	(2,332,0

See accompanying notes to consolidated financial statements.

Table of Contents

ADVENTRX Pharmaceuticals, Inc. and Subsidiaries
(A Development Stage Enterprise)
Consolidated Statements of Stockholders Equity (Deficit) and Comprehensive Loss
Inception (June 12, 1996) Through December 31, 2010

Cumulative convertible preferred stock, series A through C		Convertible preferred stock, series A (2009)		Cumulative convertible preferred stock, series B through F (2009 - 2010)		Common stock		Additional paid-in capital	Accumulated other comprehensive income (loss)	Deficit accumulated during the development stage	Treasury stock, at cost	Total stockholders equity (deficit)	Co
Shares	Amount	Shares	Amount	Shares	Amount	Shares	Amount						
													ent
	$		$		$		$	$ 72,800	$	$	$	$ 72,800	
													ck f
(473)	(4)					9,460	9	(5)					ck f erred
(200,000)	(2,000)					8,000	8	1,992					rcise
						18,583	18	(18)					
						953	1	27,352				27,353	
								86,375				86,375	a non 0 per
						416,705	417	15,626,033				15,626,450	
								(1,366,774)				(1,366,774)	l s tock
								524,922				524,922	
								34,747			(34,747)		

					(6,701,048)		(6,701,048) $
	2,153,369	2,153	47,605,179		(35,182,194)	(34,747)	12,390,391 $
					(24,782,646)		(24,782,646) $
				(1,722)			(1,722)
	432,432	433	(433)				
	5,985	6	(6)				
	90,348	90	3,073,348				3,073,438
	7,400	7	144,993				145,000
			994,874				994,874
			93,549				93,549
	5,000	5	258,495				258,500
	2,694,534	2,694	52,169,999	(1,722)	(59,964,840)	(34,747)	(7,828,616) $
					(29,331,773)		(29,331,773) $
				(368)			(368)
	16,807	17	(17)				

of ts f SD als.	204,150	204	7,691,386				7,691,590	
non 5 per	84,000	84	10,163,868				10,163,952	
s tock	581,800	582	37,069,629				37,070,211	
	2,406	2	196,672				196,674	
tock	3,700	4	125,747				125,751	
ck to es tock	600	1	68,649				68,650	
tock			1,697,452				1,697,452	
e of k			104,225				104,225	
	(927)	(1)	(34,746)			34,747		
, ted	3,587,070	3,587	109,252,864	(2,090)	(89,296,613)		19,957,748	$
ffect								
			18,116,751		12,239,688		30,356,439	
					(22,142,040)		(22,142,040)	$
nge of sale				4,792			4,792	
tock	23,033	23	441,593				441,616	
tock			2,414,077				2,414,077	
tock			1,908				1,908	

3,610,103	3,610	130,227,193	2,702	(99,198,965)	31,034,540	$

See accompanying notes to consolidated financial statements.

Table of Contents

ADVENTRX Pharmaceuticals, Inc. and Subsidiaries
(A Development Stage Enterprise)
Consolidated Statements of Stockholders Equity (Deficit) and Comprehensive Loss
Inception (June 12, 1996) Through December 31, 2010

Cumulative convertible preferred stock, series A through C		Convertible preferred stock, series A (2009)		Cumulative convertible preferred stock, series B through F (2009 - 2010)		Common stock		Additional paid-in capital	Accumulated other comprehensive income (loss)	Deficit accumulated during the development stage	Treasury stock, at cost	Total stockholders equity (deficit)	Co
Shares	Amount	Shares	Amount	Shares	Amount	Shares	Amount						
	$		$		$		$	$	$	$ (26,647,493)	$	$ (26,647,493)	$
nge of -sale									(2,702)			(2,702)	
tock													
tock													
								1,605,908				1,605,908	
tock													
e								4,982				4,982	
,						3,610,103	3,610	131,838,083		(125,846,458)		5,995,235	$
										(11,325,058)		(11,325,058)	$
A ck, g ,125 f erred		1,993	2					1,735,627				1,735,629	
ck		(1,993)	(2)			721,448	721	(719)					
				1,361	1			833,030				833,031	

B ck, g ,643 f erred								
ck	(1,361)	(1)	380,168	380	(379)			
C ck, g ,885 f erred	922	1			711,198			711,199
ck	(922)	(1)	283,692	284	(283)			
D ck, g								
	11,283	11			5,124,125			5,124,136
f erred								
ck dend	(11,283)	(11)	2,400,000	2,400	(2,389)			
ck dend					1,207,536	(1,207,536)		
ck dend					214,795	(214,795)		
ck dend					186,173	(186,173)		
ck tock					3,258,383	(3,258,383)		
rants					585,438			585,438
rants			240,000	240	899,760			900,000
			576,000	576	2,113,344			2,113,920
,			8,211,411	8,211	148,703,722	(142,038,403)	6,673,530	$

							(8,450,922)	(8,450,922)	$
sh or ares e									
			(31)		(146)			(146)	
E ck, g									
	19,000	19			14,014,705			14,014,724	
f erred									
ck F	(19,000)	(19)	1,993,965	1,994	(1,975)				
ck, g									
	19,217	19			13,344,749			13,344,768	
f erred									
ck dend	(19,217)	(19)	5,190,306	5,190	(5,171)				
ck dend					2,514,920		(2,514,920)		
ck tock					3,124,876		(3,124,876)		
					785,943			785,943	
rants			84,651	85	317,359			317,444	
,									
$	$	$	15,480,302	$ 15,480	$ 182,798,982	$	$ (156,129,121)	$ $ 26,685,341	$

See accompanying notes to consolidated financial statements.

Table of Contents

ADVENTRX Pharmaceuticals, Inc. and Subsidiaries
(A Development Stage Enterprise)
Consolidated Statements of Cash Flows

	Years Ended December 31,		Inception (June 12, 1996) Through December 31,
	2010	2009	2010
Cash flows from operating activities:			
Net loss	$ (8,450,922)	$ (11,325,058)	$ (158,357,728)
Adjustments to reconcile net loss to net cash used in operating activities:			
Depreciation and amortization	19,821	79,728	10,447,620
Loss on disposal of fixed assets	4,269	59,114	59,785
Loss on fair value of warrants			12,239,688
Amortization of debt discount			450,000
Forgiveness of employee receivable			30,036
Impairment loss write-off of goodwill			5,702,130
Expenses related to employee stock options and restricted stock issued	785,943	585,437	9,223,942
Expenses related to options issued to non-employees			204,664
Expenses paid by issuance of common stock			1,341,372
Expenses paid by issuance of warrants			573,357
Expenses paid by issuance of preferred stock			142,501
Expenses related to stock warrants issued			612,000
Equity in loss of investee			178,936
In-process research and development			10,422,130
Write-off of license agreement			152,866
Write-off assets available-for-sale			108,000
Cumulative effect of change in accounting principle			25,821
Accretion of discount on investments in securities			(1,604,494)
Changes in assets and liabilities, net of effect of acquisitions:			
(Increase) decrease in prepaid and other assets	(148,137)	344,699	(711,110)
Increase (decrease) in accounts payable and accrued liabilities	(552,211)	(2,360,336)	1,978,184
Net cash used in operating activities	(8,341,237)	(12,616,416)	(106,780,300)
Cash flows from investing activities:			
Proceeds from sales and maturities of short-term investments			112,788,378
Purchases of short-term investments			(111,183,884)
Purchases of property and equipment	(28,513)		(1,058,867)
Proceeds from sale of property and equipment	4,379	16,000	54,285
Purchase of certificate of deposit			(1,016,330)

Table of Contents

ADVENTRX Pharmaceuticals, Inc. and Subsidiaries
(A Development Stage Enterprise)
Consolidated Statements of Cash Flows

	Years Ended December 31, 2010	2009	Inception (June 12, 1996) Through December 31, 2010
Maturity of certificate of deposit	$	$	$ 1,016,330
Cash paid for acquisitions, net of cash acquired			32,395
Payment on obligation under license agreement			(106,250)
Issuance of note receivable related party			(35,000)
Payments on note receivable			405,993
Advance to investee			(90,475)
Cash transferred in rescission of acquisition			(19,475)
Cash received in rescission of acquisition			230,000
Net cash provided by (used in) investing activities	(24,134)	16,000	1,017,100
Cash flows from financing activities:			
Proceeds from sale of common stock			84,151,342
Proceeds from exercise of stock options			712,367
Proceeds from sale or exercise of warrants	317,444	3,013,920	14,714,258
Proceeds from sale of preferred stock	30,453,227	9,820,500	44,474,720
Repurchase of warrants			(55,279)
Payments for financing and offering costs	(3,093,735)	(1,416,504)	(10,994,048)
Payments on notes payable and long-term debt			(605,909)
Proceeds from issuance of notes payable and detachable warrants			1,344,718
Cash paid in lieu of fractional shares for reverse stock split	(146)		(146)
Net cash provided by financing activities	27,676,790	11,417,916	133,742,023
Net increase (decrease) in cash	19,311,419	(1,182,500)	27,978,823
Cash at beginning of period	8,667,404	9,849,904	
Cash at end of period	$ 27,978,823	$ 8,667,404	$ 27,978,823

See accompanying notes to consolidated financial statements.

Table of Contents

ADVENTRX Pharmaceuticals, Inc. and Subsidiaries
(A Development Stage Enterprise)
Notes to Consolidated Financial Statements
December 31, 2010

(1) Description of Business

ADVENTRX Pharmaceuticals, Inc., a Delaware corporation (ADVENTRX, we or the Company), is a specialty pharmaceutical company focused on acquiring, developing and commercializing proprietary product candidates. We have devoted substantially all of our resources to research and development (R&D), or to acquisition of our product candidates. We have not yet marketed or sold any products or generated any significant revenue.

Through our acquisition of SD Pharmaceuticals, Inc. (SDP) in 2006, we have rights to product candidates in varying stages of development, including our lead product candidates, Exelbine (vinorelbine injectable emulsion) and ANX-514 (docetaxel emulsion for injection), which are novel emulsion formulations of currently marketed chemotherapy drugs. In February 2011, we entered into an agreement and plan of merger to acquire SynthRx, Inc., a privately-held Delaware corporation in exchange for shares of our common stock. See Note 17, Subsequent Events, below for additional information regarding this pending acquisition.

In October 2000, we merged our wholly-owned subsidiary, Biokeys Acquisition Corp., with and into Biokeys, Inc. and changed our name to Biokeys Pharmaceuticals, Inc. In May 2003, we merged Biokeys Inc., our wholly-owned subsidiary, with and into us and changed our name to ADVENTRX Pharmaceuticals, Inc. The merger had no effect on our financial statements. In July 2004, we formed a wholly-owned subsidiary, ADVENTRX (Europe) Ltd., in the United Kingdom primarily to facilitate conducting clinical trials in the European Union, but we dissolved this subsidiary in December 2009. In April 2006, we acquired all of the outstanding capital stock of SDP through a merger with our newly created wholly-owned subsidiary, Speed Acquisition, Inc. (the Merger Sub) and changed the name of the Merger Sub to SD Pharmaceuticals, Inc.

(2) Summary of Significant Accounting Policies

Basis of Presentation

The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries, SDP and ADVENTRX (Europe) Ltd. up until its dissolution in December 2009. All intercompany accounts and transactions have been eliminated in consolidation.

On April 23, 2010, the Company effected a 1-for-25 reverse split of its common stock, which was authorized by its stockholders at a special meeting held in August 2009. All common stock share and per share information in the consolidated financial statements and notes thereto included in this report have been restated to reflect retrospective application of the reverse stock split for all periods presented ending or as of a date prior to April 23, 2010, except for par value per share and the number of authorized shares, which were not affected by the reverse stock split.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America (U.S.) requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying notes. Actual results could differ from those estimates.

Cash Equivalents

Cash equivalents consist of highly liquid investments with original maturities of three months or less at the date of purchase. The carrying amounts approximate fair value due to the short maturities of these instruments. At December 31, 2010 and 2009, we did not have any cash equivalents.

Table of Contents

ADVENTRX Pharmaceuticals, Inc. and Subsidiaries
(A Development Stage Enterprise)
Notes to Consolidated Financial Statements
December 31, 2010

Concentrations

Financial instruments that potentially subject us to concentrations of credit risk consist principally of cash and cash equivalents and investment securities. We maintain our cash and cash equivalents in high-credit quality financial institutions. At times, such balances exceed federally insured limits. At December 31, 2010 and 2009, our cash was in excess of the Federal Deposit Insurance Corporation limit and we did not have any cash equivalents or investment securities.

During 2010, approximately 13% or $1.4 million of our total vendor payments were made to a manufacturer that provided process development and scale-up manufacturing services that assisted us in completing a New Drug Application (NDA) for our lead product candidate, ANX-530, which we filed with the United States Food and Drug Administration (FDA) in November 2010. If we were to lose this vendor, our progress toward commercializing Exelbine would be severely impeded. This vendor also provides process development and scale-up manufacturing services for our other lead product candidate, ANX-514; however, we are evaluating alternate vendors with respect to ANX-514. During 2009, approximately 28% or $3.5 million of our total vendor payments were made to the same manufacturer.

Property and Equipment

Property and equipment are stated at cost. Depreciation and amortization are calculated using the straight-line method over the estimated useful lives of the assets. The costs of improvements that extend the lives of the assets are capitalized. Repairs and maintenance are expensed as incurred.

Impairment of Long-Lived Assets

Long-lived assets with finite lives are evaluated for impairment whenever events or changes in circumstances indicate that their carrying value may not be recoverable. If the evaluation indicates that intangibles or long-lived assets are not recoverable (i.e., carrying amount is less than the future projected undiscounted cash flows), their carrying amount would be reduced to fair value. Since inception through December 31, 2010, we recognized an impairment loss of the value of goodwill in the amount of $5.7 million, which was recorded in the year ended December 31, 2001.

Revenue Recognition

We may enter into revenue arrangements that contain multiple deliverables. In these cases, revenue is recognized when all of the following criteria are met: (1) persuasive evidence of an arrangement exists; (2) delivery has occurred or services have been rendered; (3) the seller s price to the buyer is fixed and determinable; and (4) collectability is reasonably assured.

Revenue from licensing agreements is recognized based on the performance requirements of the agreement. Revenue is deferred for fees received before earned. Nonrefundable upfront fees that are not contingent on any future performance by us are recognized as revenue when the revenue recognition criteria are met and the license term commences. Nonrefundable upfront fees, where we have ongoing involvement or performance obligations, are recorded as deferred revenue and recognized as revenue over the life of the contract, the period of the performance obligation or the development period, whichever is appropriate in light of the circumstances. Payments related to substantive, performance-based milestones in an agreement are recognized as revenue upon the achievement of the milestones as specified in the underlying agreement when they represent the culmination of the earnings process. Royalty revenue from licensed products will be recognized when earned in accordance with the terms of the applicable license agreements.

Table of Contents

ADVENTRX Pharmaceuticals, Inc. and Subsidiaries
(A Development Stage Enterprise)
Notes to Consolidated Financial Statements
December 31, 2010

We recognize revenues from federal government research grants during the period in which we receive the grant funds, or their collection is reasonably assured, and we incur the qualified expenditures.

Research and Development Expenses

Research and development (R&D) expenses consist of expenses incurred in performing R&D activities, including salaries and benefits, facilities and other overhead expenses, bioequivalence and clinical trials, research-related manufacturing services, contract services and other outside expenses. R&D expenses are charged to operations as they are incurred. Advance payments, including nonrefundable amounts, for goods or services that will be used or rendered for future R&D activities are deferred and capitalized. Such amounts will be recognized as an expense as the related goods are delivered or the related services are performed. If the goods will not be delivered, or services will not be rendered, then the capitalized advance payment is charged to expense.

Milestone payments that we make in connection with in-licensed technology or product candidates are expensed as incurred when there is uncertainty in receiving future economic benefits from the licensed technology or product candidates. We consider the future economic benefits from the licensed technology or product candidates to be uncertain until such licensed technology is incorporated into products that, or such product candidates, are approved for marketing by the FDA or when other significant risk factors are abated. For expense accounting purposes, management has viewed future economic benefits for all of our licensed technology or product candidates to be uncertain.

Payments in connection with our bioequivalence and clinical trials are often made under contracts with multiple clinical research organizations (CROs) that conduct and manage these trials on our behalf. The financial terms of these agreements are subject to negotiation and vary from contract to contract and may result in uneven payment flows. Generally, these agreements set forth the scope of work to be performed at a fixed fee or unit price or on a time-and-material basis. Payments under these contracts depend on factors such as the successful enrollment or treatment of patients or the completion of other milestones. Expenses related to bioequivalence and clinical trials are accrued based on our estimates and/or representations from service providers regarding work performed, including actual level of patient enrollment, completion of patient studies, and trials progress. Other incidental costs related to patient enrollment and treatment are accrued when reasonably certain. If the contracted amounts are modified (for instance, as a result of changes in the bioequivalence or clinical trial protocol or scope of work to be performed), we modify our accruals accordingly on a prospective basis. Revisions in scope of contract are charged to expense in the period in which the facts that give rise to the revision become reasonably certain. Because of the uncertainty of possible future changes to the scope of work in bioequivalence and clinical trials contracts, we are unable to quantify an estimate of the reasonably likely effect of any such changes on our consolidated results of operations or financial position. Historically, we have had no material changes in our bioequivalence or clinical trial expense accruals that would have had a material impact on our consolidated results of operations or financial position.

Purchased In-Process Research and Development

In accordance with previous accounting guidance effective through December 31, 2008, we immediately charged the costs associated with in-process research and development (IPR&D) purchased prior to December 31, 2008 to the statement of operations upon acquisition. These amounts represented an estimate of the fair value of purchased IPR&D for projects that, as of the acquisition date, had not yet reached technological feasibility, had no alternative future use, and had uncertainty in receiving future economic benefits from the purchased IPR&D. We determined the future economic benefits from the purchased IPR&D to be uncertain until such technology is incorporated into products approved by the FDA or when other significant risk factors are abated. In the year ended December 31, 2006, we recorded approximately $10.4 million of IPR&D expense related to our acquisition of SD Pharmaceuticals, Inc. in April 2006.

Table of Contents

ADVENTRX Pharmaceuticals, Inc. and Subsidiaries
(A Development Stage Enterprise)
Notes to Consolidated Financial Statements
December 31, 2010

We will account for future purchased IPR&D in accordance with the Financial Accounting Standards Board s (FASB) updated guidance for business combinations, which became effective January 1, 2009.

Share-Based Compensation

Share-based compensation cost is measured at the grant date, based on the estimated fair value of the award and is recognized as expense over the employee s requisite service period on a straight-line basis. Share-based compensation expense recognized in the consolidated statements of operations for the years ended December 31, 2010 and 2009 is based on awards ultimately expected to vest and has been reduced for estimated forfeitures. This estimate will be revised in subsequent periods if actual forfeitures differ from those estimates. We have no awards with market or performance conditions.

Patent Costs

Legal costs in connection with approved patents and patent applications are expensed as incurred and classified as selling, general and administrative expense in our consolidated statement of operations.

Income Taxes

We account for income taxes and the related accounts under the liability method. Deferred tax assets and liabilities are determined based on the differences between the financial statement carrying amounts and the income tax basis of assets and liabilities. A valuation allowance is applied against any net deferred tax asset if, based on available evidence, it is more likely than not that some or all of the deferred tax assets will not be realized.

The tax effects from an uncertain tax position can be recognized in our consolidated financial statements only if the position is more likely than not of being sustained upon an examination by tax authorities. An uncertain income tax position will not be recognized if it has less than a 50% likelihood of being sustained.

We account for interest and penalties related to income tax matters in income tax expense.

Comprehensive Loss

Comprehensive income or loss is defined as the change in equity of a business enterprise during a period from transactions and other events and circumstances from non-owner sources, including foreign currency translation adjustments and unrealized gains and losses on marketable securities. We present comprehensive loss in our consolidated statements of stockholders equity (deficit) and comprehensive loss.

Net Loss per Common Share

Basic and diluted net loss per common share was calculated by dividing the net loss applicable to common stock for the period by the weighted-average number of common shares outstanding during the period, without consideration for our outstanding common stock equivalents because their effect would have been anti-dilutive. Common stock equivalents are included in the calculation of diluted earnings per common share only if their effect is dilutive. As of December 31, 2010 and 2009, our outstanding common stock equivalents consisted of options and warrants as follows:

	2010	**2009**
Warrants	4,055,030	946,344
Options	403,737	234,356
	4,458,767	1,180,700

Table of Contents

ADVENTRX Pharmaceuticals, Inc. and Subsidiaries
(A Development Stage Enterprise)
Notes to Consolidated Financial Statements
December 31, 2010

Supplemental Cash Flow Information

	Years Ended December 31, 2010	2009	Inception (June 12, 1996) Through December 31, 2010
Supplemental disclosures of cash flow information:			
Interest paid	$ 1,629	$	$ 180,719
Income taxes paid			
Supplemental disclosures of non-cash investing and financing activities:			
Issuance of warrants, common stock and preferred stock for:			
Conversion of notes payable and accrued interest			1,213,988
Prepaid services to consultants			1,482,781
Conversion of preferred stock	7,184	3,785	13,674
Acquisitions			24,781,555
Payment of dividends			213,000
Financial advisor services in conjunction with private placements	724,286	691,812	2,553,554
Acquisition of treasury stock in settlement of a claim			34,737
Cancellation of treasury stock			(34,737)
Assumptions of liabilities in acquisitions			1,235,907
Acquisition of license agreement for long-term debt			161,180
Cashless exercise of warrants			4,312
Dividends accrued			621,040
Trade asset converted to available for sale asset			108,000
Dividends extinguished			408,240
Trade payable converted to note payable			83,948
Issuance of warrants for return of common stock			50,852
Detachable warrants issued with notes payable			450,000
Cumulative preferred stock dividends	7,763,903	5,738,500	13,502,403

Recent Accounting Pronouncements

In October 2009, the FASB issued Accounting Standard Update (ASU) No. 2009-13, Revenue Recognition (ASC 605) Multiple-Deliverable Revenue Arrangements, a consensus of the FASB Emerging Issues Task Force. The guidance modifies the fair value requirements of Accounting Standards Codification (ASC) subtopic 605-25 Revenue Recognition Multiple Element Arrangements by providing principles for allocation of consideration among its multiple elements, allowing more flexibility in identifying and accounting for separate deliverables under an arrangement. An estimated selling price method is introduced for valuing the elements of a bundled arrangement if vendor-specific objective evidence or third-party evidence of selling price is not available, and significantly expands related disclosure requirements. This guidance is effective prospectively for revenue arrangements entered into or materially modified in fiscal years beginning on or after June 15, 2010. Currently, we have no multiple-deliverable revenue arrangements that would be affected by this guidance.

In March 2010, the FASB ratified the milestone method of revenue recognition. Under this standard, an entity can recognize contingent consideration earned from the achievement of a substantive milestone in its entirety in

the period in which the milestone is achieved. A milestone is defined as an event (i) that can only be achieved based in whole or in part on either the entity s performance or on the occurrence of a specific outcome resulting from the entity s performance (ii) for which there is substantive uncertainty at the date the arrangement is entered into that the event will be achieved and (iii) that would result in additional payments being due to the entity. This guidance is effective for years beginning after June 15, 2010. We are evaluating the effect, if any, that this guidance will have on our financial position or results of operations.

Table of Contents

ADVENTRX Pharmaceuticals, Inc. and Subsidiaries
(A Development Stage Enterprise)
Notes to Consolidated Financial Statements
December 31, 2010

(3) Fair Value Measurements

The guidance for the fair value option for financial assets and financial liabilities provides companies the irrevocable option to measure many financial assets and liabilities at fair value with changes in fair value recognized in earnings. We have not elected to measure any financial assets or liabilities at fair value that were not previously required to be measured at fair value.

Fair value is defined as the exit price, or the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants as of the measurement date. The guidance also establishes fair value hierarchy for inputs used in measuring fair value that maximizes the use of observable inputs and minimizes the use of unobservable inputs by requiring that the most observable inputs be used when available. Observable inputs are inputs market participants would use in valuing the asset or liability and are developed based on market data obtained from sources independent of the Company. Unobservable inputs are inputs that reflect the Company s assumptions about the factors market participants would use in valuing the asset or liability. The guidance establishes three levels of inputs that may be used to measure fair value as follows:

Level 1 Quoted prices in active markets for identical assets or liabilities.

Level 2 Inputs other than Level 1 that are observable, either directly or indirectly, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.

Level 3 Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities.

At December 31, 2010 and 2009, we had no financial assets or liabilities required to be measured at fair value.

(4) Property and Equipment

Property and equipment at December 31, 2010 and 2009 were as follows:

	Useful Lives	2010	2009
Office furniture, computer and lab equipment	3 - 5 years	$ 216,698	$ 293,480
Computer software	3 years	60,841	89,422
Leasehold improvements	1 year	21,733	
		299,272	382,902
Less accumulated depreciation and amortization		(255,018)	(338,692)
Property and equipment, net		$ 44,254	$ 44,210

At December 31, 2010, there was $14,165 of lab equipment held for sale with an equipment reseller on a consignment basis.

Depreciation and amortization expense was $19,821 and $79,728 for the years ended December 31, 2010 and 2009, respectively.

Table of Contents

ADVENTRX Pharmaceuticals, Inc. and Subsidiaries
(A Development Stage Enterprise)
Notes to Consolidated Financial Statements
December 31, 2010

(5) Accrued Liabilities

Accrued liabilities at December 31, 2010 and 2009 were as follows:

	2010	2009
Accrued contracts and study expenses	$ 381,309	$ 1,144,279
Other accrued liabilities	483,548	234,731
Accrued liabilities	$ 864,857	$ 1,379,010

(6) Capital Stock and Warrants

Reverse Stock Split

At a special meeting of our stockholders held on August 25, 2009, our stockholders approved a proposal to authorize our board of directors, in its discretion, to effect a reverse split of our outstanding common stock without further action by our stockholders. In April 2010, our board of directors approved a 1-for-25 reverse split of our common stock and on April 23, 2010 at 4:01 p.m. Eastern time, the reverse stock split became effective. As a result of the reverse stock split, each 25 shares of our issued and outstanding common stock were automatically reclassified as and changed into one share of our common stock. The reverse stock split reduced the number of our issued and outstanding shares of common stock as of April 23, 2010 from approximately 257.3 million shares to approximately 10.3 million shares. No fractional shares were issued in connection with the reverse stock split. Stockholders who were entitled to fractional shares instead became entitled to receive a cash payment in lieu of receiving fractional shares (after taking into account and aggregating all shares of our common stock then held by such stockholder) equal to the fractional share interest multiplied by $4.6275 (the per share closing price of our common stock (on a post-split basis) as determined by the NYSE Amex on April 23, 2010). The reverse stock split affected all of the holders of our common stock uniformly. Shares of our common stock underlying outstanding options and warrants were proportionately reduced and the exercise prices of outstanding options and warrants were proportionately increased in accordance with the terms of the agreements governing such securities. All common stock share and per share information in the consolidated financial statements and notes thereto included in this report have been restated to reflect retrospective application of the reverse stock split for all periods presented ending or as of a date on or prior to April 23, 2010, except for par value per share and the number of authorized shares, which were not affected by the reverse stock split.

0% Series A Convertible Preferred Stock

In June 2009, we completed a registered direct equity financing raising gross proceeds of approximately $2.0 million involving the issuance of units consisting of 1,993 shares of our 0% Series A Convertible Preferred Stock with a stated value of $1,000 per share (Series A Stock) and 5-year warrants to purchase up to 324,651 shares of our common stock at an exercise price of $3.75 per share. In the aggregate, the shares of Series A Stock we issued were convertible into 721,448 shares of our common stock. All of the shares of the Series A Stock have been converted into common stock and are no longer outstanding. We received approximately $1.7 million in net proceeds from the financing, after deducting the placement agent s fees and expenses and other offering expenses. In December 2009, in connection with the exercise of warrants issued in the June 2009 financing, we issued 240,000 shares of our common stock and received net proceeds of $0.9 million. In January 2010, in connection with the exercise of the remaining warrants issued in the June 2009 financing, we issued an additional 84,651 shares of our common stock and received an additional $0.3 million of net proceeds. All of the warrants we issued in the June 2009 financing have been exercised and are no longer outstanding.

Table of Contents

ADVENTRX Pharmaceuticals, Inc. and Subsidiaries
(A Development Stage Enterprise)
Notes to Consolidated Financial Statements
December 31, 2010

The convertible feature of our Series A Stock and the terms of the warrants issued in connection with our Series A Stock provided for a rate of conversion or exercise that was below the market value of our common stock at issuance. The convertible feature of our Series A Stock is characterized as a beneficial conversion feature (BCF). The estimated relative fair values of the shares of our Series A Stock and the warrants issued in connection with such stock were calculated as approximately $1.2 million and $531,000, respectively. The value of the BCF was determined using the intrinsic value method and calculated as approximately $1.2 million. Because our Series A Stock did not have a stated redemption date, the value of the BCF was fully realized at the time our Series A Stock was issued. The fair value of the warrants was determined using the Black-Scholes option-pricing model as of the date of issuance assuming a five-year term, stock volatility of 197.01%, and a risk-free interest rate of 2.81%. The value of the BCF was treated as a deemed dividend to the holders of our Series A Stock and, due to the potential immediate convertibility of our Series A Stock at issuance, was recorded as an increase to additional paid-in capital and accumulated deficit at the time of issuance.

We also issued warrants to purchase up to 36,071 shares of our common stock at an exercise price of $3.75 per share to the placement agent in the June 2009 financing as additional consideration for its services in connection with the financing. These warrants had a fair value of approximately $132,000 using the Black-Scholes option-pricing model as of the date of issuance assuming a five-year term, stock volatility of 196.5%, and a risk-free interest rate of 2.85%. The warrants became exercisable on December 13, 2009 and are exercisable at any time on or before June 12, 2014.

5% Series B Convertible Preferred Stock

In July 2009, we completed a registered direct equity financing raising gross proceeds of approximately $1.4 million involving the issuance of 1,361 shares of our 5% Series B Convertible Preferred Stock with a stated value of $1,000 per share (Series B Stock). In the aggregate, the shares of Series B Stock we issued were convertible into 380,168 shares of our common stock. All of the shares of our Series B Stock have been converted into common stock and are no longer outstanding. Our Series B Stock would have accrued a cumulative annual dividend of 5% per share until July 6, 2014, and no dividend thereafter. In accordance with the terms of the Series B Stock, because the Series B Stock was converted prior to July 6, 2014, we paid the holders an amount equal to the total dividend that would have accrued in respect of the shares converted from the issuance date through July 6, 2014, or $250 per $1,000 of stated value of the shares converted. We received approximately $0.8 million in net proceeds from the financing after deducting the $340,250 we placed into escrow accounts to pay the aggregate dividend payment in respect of our Series B Stock, placement agent s fees and expenses and other offering expenses.

The convertible feature of our Series B Stock and the value of the dividend in respect thereof provided for a rate of conversion that was below the market value of our common stock at issuance. The convertible feature of our Series B Stock is characterized as a BCF. The estimated relative fair value of the shares of our Series B Stock was calculated as approximately $1.0 million. The value of the BCF was determined using the intrinsic value method and calculated as approximately $215,000. Because our Series B Stock did not have a stated redemption date, the value of the BCF was fully realized at the time our Series B Stock was issued. The value of the BCF was treated as a deemed dividend to the holders of our Series B Stock and, due to the potential immediate convertibility of our Series B Stock at issuance, was recorded as an increase to additional paid-in capital and accumulated deficit at the time of issuance.

We also issued warrants to purchase up to 19,007 shares of our common stock at an exercise price of $4.48 per share to the placement agent in the July 2009 financing as additional consideration for its services in connection with the financing. These warrants had a fair value of approximately $60,000 using the Black-Scholes option-pricing model as of the date of issuance assuming a five-year term, stock volatility of 197.37%, and a risk-free interest rate of 2.4%. The warrants became exercisable on January 7, 2010 and are exercisable at any time on or before July 6, 2014.

Table of Contents

ADVENTRX Pharmaceuticals, Inc. and Subsidiaries
(A Development Stage Enterprise)
Notes to Consolidated Financial Statements
December 31, 2010

5% Series C Convertible Preferred Stock

In August 2009, we completed a registered direct equity financing raising gross proceeds of approximately $0.9 million involving the issuance of 922 shares of our 5% Series C Convertible Preferred Stock with a stated value of $1,000 per share (Series C Stock). In the aggregate, the shares of Series C Stock we issued were convertible into 283,692 shares of our common stock. All of the shares of our Series C Stock have been converted into common stock and are no longer outstanding. Our Series C Stock would have accrued a cumulative annual dividend of 5% per share until February 10, 2012, and no dividend thereafter. In accordance with the terms of the Series C Stock, because the Series C Stock was converted prior to February 10, 2012, we paid the holders an amount equal to the total dividend that would have accrued in respect of the shares converted from the issuance date through February 10, 2012, or $125 per $1,000 of stated value of the shares converted. We received approximately $0.7 million in net proceeds from the financing after deducting the $115,250 we placed into escrow accounts to pay the aggregate dividend payment in respect of our Series C Stock, placement agent s fees and expenses and other offering expenses.

The convertible feature of our Series C Stock and the value of the dividend in respect thereof provided for a rate of conversion that was below the market value of our common stock at issuance. The convertible feature of our Series C Stock is characterized as a BCF. The estimated relative fair value of the shares of our Series C Stock was calculated as approximately $807,000. The value of the BCF was determined using the intrinsic value method and calculated as approximately $186,000. Because our Series C Stock did not have a stated redemption date, the value of the BCF was fully realized at the time our Series C Stock was issued. The value of the BCF was treated as a deemed dividend to the holders of our Series C Stock and, due to the potential immediate convertibility of our Series C Stock at issuance, was recorded as an increase to additional paid-in capital and accumulated deficit at the time of issuance.

We also issued warrants to purchase up to 14,183 shares of our common stock at an exercise price of $4.06 per share to the placement agent in the August 2009 financing as additional consideration for its services in connection with the financing. These warrants had a fair value of approximately $48,000 using the Black-Scholes option-pricing model as of the date of issuance assuming a five-year term, stock volatility of 198.94%, and a risk-free interest rate of 2.75%. The warrants became exercisable on February 10, 2010 and are exercisable at any time on or before August 10, 2014.

4.25660% Series D Convertible Preferred Stock

In October 2009, we completed a registered direct equity financing raising gross proceeds of approximately $11.3 million involving the issuance of units consisting of 11,283 shares of our 4.25660% Series D Convertible Preferred Stock with a stated value of $1,000 per share (Series D Stock) and 5-year warrants to purchase up to an aggregate of 792,000 shares of our common stock. In the aggregate, the shares of Series D Stock we issued were convertible into 2,400,000 shares of our common stock. All of the shares of our Series D Stock have been converted into common stock and are no longer outstanding. Our Series D Stock would have accrued a cumulative annual dividend of 4.25660% per share until October 9, 2020, and no dividend thereafter. In accordance with the terms of the Series D Stock, because the Series D Stock was converted prior to October 9, 2020, we paid the holders an amount equal to the total dividend that would have accrued in respect of the shares converted from the issuance date through October 9, 2020, or $468.23 per $1,000 of stated value of the shares converted. We received approximately $5.1 million in net proceeds from the financing after deducting the approximately $5.3 million we placed into escrow accounts to pay the aggregate dividend payment in respect of our Series D Stock, placement agent s fees and expenses and other offering expenses. In December 2009, in connection with the exercise of warrants issued in the October 2009 financing, we issued 576,000 shares of our common stock and received net proceeds of $2.1 million. We may receive an additional $0.8 million of net proceeds from the exercise of the remaining warrants issued in the October 2009 financing. Those warrants, which have an exercise price of $3.67 per share, are exercisable any time on or before October 9, 2014, subject to

certain beneficial ownership limitations.

Table of Contents

ADVENTRX Pharmaceuticals, Inc. and Subsidiaries
(A Development Stage Enterprise)
Notes to Consolidated Financial Statements
December 31, 2010

The convertible feature of our Series D Stock and the terms of the warrants issued in connection with our Series D Stock provide for a rate of conversion or exercise that was below the market value of our common stock at issuance. The convertible feature of our Series D Stock is characterized as BCF. The estimated relative fair values of the shares of our Series D Stock and the warrants issued in connection with such stock were calculated as approximately $3.9 million and $1.3 million, respectively. The value of the BCF was determined using the intrinsic value method and calculated as approximately $3.3 million. Because our Series D Stock did not have a stated redemption date, the value of the BCF was fully realized at the time our Series D Stock was issued. The fair value of the warrants was determined using the Black-Scholes option-pricing model as of the date of issuance assuming a five-year term, stock volatility of 197.63%, and a risk-free interest rate of 2.36%. The value of the BCF was treated as a deemed dividend to the holders of our Series D Stock and, due to the potential immediate convertibility of our Series D Stock at issuance, was recorded as an increase to additional paid-in capital and accumulated deficit at the time of issuance.

We also issued warrants to purchase up to 144,000 shares of our common stock at an exercise price of $5.88 per share to the placement agent in the October 2009 financing as additional consideration for its services in connection with the financing. These warrants had a fair value of approximately $452,000 using the Black-Scholes option-pricing model as of the date of issuance assuming a five-year term, stock volatility of 197.63%, and a risk-free interest rate of 2.36%. The warrants became exercisable on April 7, 2010 and are exercisable at any time on or before October 6, 2014.

3.73344597664961% Series E Convertible Preferred Stock

In January 2010, we completed a registered direct equity financing raising gross proceeds of $19.0 million involving the issuance of units consisting of 19,000 shares of our 3.73344597664961% Series E Convertible Preferred Stock with a stated value of $1,000 per share (Series E Stock) and 30-month warrants to purchase up to an aggregate of 498,488 shares of our common stock. In the aggregate, the shares of Series E Stock we issued were convertible into 1,993,965 shares of our common stock. All of the shares of our Series E Stock have been converted into common stock and are no longer outstanding. Our Series E Stock would have accrued a cumulative annual dividend of 3.73344597664961% per share until January 7, 2015, and no dividend thereafter. In accordance with the terms of the Series E Stock, because the Series E Stock was converted prior to January 7, 2015, we paid the holders an amount equal to the total dividend that would have accrued in respect of the shares converted from the issuance date through January 7, 2015, or $186.67 per $1,000 of stated value of the shares converted. We received approximately $14.0 million in net proceeds from the financing after deducting the approximately $3.5 million we placed into escrow accounts to pay the aggregate dividend payment in respect of our Series E Stock, placement agent s fees and expenses and other offering expenses. We may receive up to approximately $4.4 million of additional proceeds from the exercise of the warrants issued in the January 2010 financing. Those warrants, which have an exercise price of $8.75 per share, are exercisable any time on or before July 6, 2012, subject to certain beneficial ownership limitations.

The convertible feature of our Series E Stock and the terms of the warrants issued in connection with our Series E Stock provide for a rate of conversion or exercise that was below the market value of our common stock at issuance. The convertible feature of our Series E Stock is characterized as BCF. The estimated relative fair values of the shares of our Series E Stock and the warrants issued in connection with such stock were calculated as approximately $12.4 million and $3.0 million, respectively. The value of the BCF was determined using the intrinsic value method and calculated as approximately $2.5 million. Because our Series E Stock did not have a stated redemption date, the value of the BCF was fully realized at the time our Series E Stock was issued. The fair value of the warrants was determined using the Black-Scholes option-pricing model as of the date of issuance assuming a 30-month term, stock volatility of 275.79%, and a risk-free interest rate of 1.325%. The value of the BCF was treated as a deemed dividend to the holders of our Series E Stock and, due to the potential immediate convertibility of our Series E Stock at issuance, was recorded as an increase to additional paid-in capital and

accumulated deficit at the time of issuance.

Table of Contents

ADVENTRX Pharmaceuticals, Inc. and Subsidiaries
(A Development Stage Enterprise)
Notes to Consolidated Financial Statements
December 31, 2010

We also issued warrants to purchase up to 99,696 shares of our common stock at an exercise price of $11.91 per share to the placement agent in the January 2010 financing as additional consideration for its services in connection with the financing. These warrants had a fair value of approximately $724,000 using the Black-Scholes option-pricing model as of the date of issuance assuming a 4.5-year term, stock volatility of 209.46%, and a risk-free interest rate of 2.37%. The warrants became exercisable on July 7, 2010 and are exercisable at any time on or before June 3, 2014.

2.19446320054018% Series F Convertible Preferred Stock

In May 2010, we completed a registered direct equity financing raising gross proceeds of $19.2 million involving the issuance of units consisting of 19,217.13 shares of our 2.19446320054018% Series F Convertible Preferred Stock with a stated value of $1,000 per share (Series F Stock), 5-year warrants to purchase up to an aggregate of 1,816,608 shares of our common stock and 1-year warrants to purchase up to an aggregate of 778,548 shares of our common stock. In the aggregate, the shares of Series F Stock we issued were convertible into 5,190,312 shares of our common stock. All of the shares of our Series F Stock have been converted into common stock and are no longer outstanding. Series F Stock would have accrued a cumulative annual dividend of 2.19446320054018% per share until May 6, 2020, and no dividend thereafter. In accordance with the terms of the Series F Stock, because the Series F Stock was converted prior to May 6, 2020, upon conversion of the shares, we paid the holders an amount equal to the total dividend that would have accrued in respect of the shares converted from the issuance date through May 6, 2020, or $219.45 per $1,000 of stated value of the shares converted, less the amount of any dividend paid on such shares before their conversion. Dividend payments were due on January 1, April 1, July 1 and October 1. Because 2,884.57 shares of our Series F Stock were outstanding at the time of the July 1, 2010 and October 1, 2010 dividend payment dates, we paid aggregate dividends of approximately $25,300 to the holders of those outstanding shares and such previously paid amounts were subtracted from the payments due in respect of those shares at the time of their conversion. We received approximately $13.3 million in net proceeds from the financing after deducting the approximately $4.2 million we placed into escrow accounts to pay the aggregate dividend payment in respect of our Series F Stock, placement agent and financial advisor fees and other offering expenses. We may receive up to approximately $9.5 million of additional proceeds from the exercise of the warrants issued in the May 2010 financing. The exercise price of the warrants is $3.65 per share. Subject to certain beneficial ownership limitations, the 5-year warrants are exercisable any time on or before May 6, 2015 and the 1-year warrants are exercisable any time on or before May 20, 2011.

The convertible feature of our Series F Stock and the terms of the warrants issued in connection with our Series F Stock provide for a rate of conversion or exercise that was below the market value of our common stock at issuance. The convertible feature of our Series F Stock is characterized as BCF. The estimated relative fair values of the shares of our Series F Stock and the warrants issued in connection with such stock were calculated as approximately $10.1 million and $4.9 million, respectively. The value of the BCF was determined using the intrinsic value method and calculated as approximately $3.1 million. Because our Series F Stock did not have a stated redemption date, the value of the BCF was fully realized at the time our Series F Stock was issued. The fair value of the 5-year warrants was determined using the Black-Scholes option-pricing model as of the date of issuance assuming a 5-year term, stock volatility of 202%, and a risk-free interest rate of 2%. The fair value of the 1-year warrants was determined using the Black-Scholes option-pricing model as of the date of issuance assuming a 1-year term, stock volatility of 361%, and a risk-free interest rate of 0.4%. The value of the BCF was treated as a deemed dividend to the holders of our Series F Stock and, due to the potential immediate convertibility of our Series F Stock at issuance, was recorded as an increase to additional paid-in capital and accumulated deficit at the time of issuance.

Common Stock Issued for Warrants Exercised

As described above, in December 2009, we issued 240,000 shares of our common stock and received net proceeds of $0.9 million, in connection with the exercise of warrants issued in the June 2009 financing at an exercise price of $3.75.

Table of Contents

ADVENTRX Pharmaceuticals, Inc. and Subsidiaries
(A Development Stage Enterprise)
Notes to Consolidated Financial Statements
December 31, 2010

As described above, in December 2009, we issued 576,000 shares of our common stock and received net proceeds of $2.1 million in connection with the exercise of warrants issued in the October 2009 financing at an exercise price of $3.67.

As described above, in January 2010, we issued 84,651 shares of our common stock and received net proceeds of $0.3 million in connection with the exercise of the remaining warrants issued in the June 2009 financing at an exercise price of $3.75 per share.

Warrants

During 2009, warrants were issued to investors in conjunction with the Series A Stock and Series D Stock financings in June and October 2009, respectively. The Series A warrants to investors have been fully exercised as described above. In addition, warrants were issued to the placement agent in each of the Series A Stock, Series B Stock, Series C Stock and Series D Stock financings in June 2009, July 2009, August 2009 and October 2009, respectively. See details of the equity financings above.

During 2010, warrants were issued to investors in conjunction with the Series E Stock and Series F Stock financings in January 2010 and May 2010, respectively. In addition, warrants were issued to the placement agent of the Series E Stock financing in January 2010. See details of the equity financings above.

At December 31, 2010, outstanding warrants to purchase shares of common stock are as follows:

Warrants		Exercise Price	Expiration Date
432,429	$	56.5000	July 2012
36,071	$	3.7500	June 2014
19,007	$	4.4750	July 2014
14,183	$	4.0625	August 2014
216,000	$	3.6700	October 2014
144,000	$	5.8750	October 2014
498,488	$	8.7475	July 2012
99,696	$	11.9125	June 2014
1,816,608	$	3.6500	May 2015
778,548	$	3.6500	May 2011
4,055,030			

(7) Equity Incentive Plans

At December 31, 2010, we had the 2005 Equity Incentive Plan (the 2005 Plan), the 2005 Employee Stock Purchase Plan (the Purchase Plan), and the 2008 Omnibus Incentive Plan (the 2008 Plan) which are described below. The share-based compensation expense from all stock options granted that has been charged to our consolidated statements of operations in the years ended December 31, 2010 and 2009 was comprised of the following:

	Years Ended December 31, 2010	2009
Selling, general and administrative expense	$ 791,688	$ 543,868
Research and development expense	(5,745)	41,569

Share-based compensation expense before taxes			785,943		585,437
Related income tax benefits					
Share-based compensation expense		$	785,943	$	585,437
Net share-based compensation expense per common share	basic and diluted	$	0.06	$	0.13

Table of Contents

ADVENTRX Pharmaceuticals, Inc. and Subsidiaries
(A Development Stage Enterprise)
Notes to Consolidated Financial Statements
December 31, 2010

Since we have net operating loss carry forwards as of December 31, 2010, no excess tax benefits for the tax deductions related to share-based awards were recognized in the consolidated statement of operations. Additionally, no incremental tax benefits were recognized, as there were no stock options exercised in the years ended December 31, 2010 and 2009 that would have resulted in a reclassification to reduce net cash provided by operating activities with an offsetting increase in net cash provided by financing activities.

2005 Equity Incentive Plan and 2008 Omnibus Incentive Plan

The 2005 and the 2008 Plans, which are stockholder-approved, are intended to encourage ownership of shares of common stock by our directors, officers, employees, consultants and advisors and to provide additional incentive for them to promote the success of our business through the grant of share-based awards. Both plans provide for the grant of incentive and non-statutory stock options as well as share appreciation rights, restricted shares, restricted share units, performance units, shares and other share-based awards. Since the 2008 Plan was approved by the Company s stockholders in May 2008, no awards have been or will be granted under the 2005 Plan. Share-based awards are subject to terms and conditions established by our board of directors or the compensation committee of our board of directors.

As of December 31, 2010, the maximum aggregate number of shares of common stock that may be issued pursuant to or subject to the foregoing types of awards granted under the 2008 Plan is 755,348 shares. Any shares of common stock that are subject to options or stock appreciation rights granted under the 2008 Plan shall be counted against this limit as one share of common stock for every one share of common stock granted. Any shares of common stock that are subject to awards other than options or stock appreciation rights granted under the 2008 Plan shall be counted against this limit as 1.2 shares of common stock for every one share of common stock granted. If any shares of common stock subject to an award under the 2008 Plan or the 2005 Plan are forfeited, expire or are settled for cash pursuant to the terms of an award, the shares subject to the award may be used again for awards under the 2008 Plan to the extent of the forfeiture, expiration or settlement. The shares of common stock will be added back as one share for every share of common stock if the shares were subject to options or stock appreciation rights granted under the 2008 Plan or under the 2005 Plan, and as 1.2 shares for every share of common stock if the shares were subject to awards other than options or stock appreciation rights granted under the 2008 Plan or the 2005 Plan. The following shares of common stock will not be added to the shares issuable under the 2008 Plan: (i) shares tendered by the participant or withheld by the Company in payment of the purchase price of an option, (ii) shares tendered by the participant or withheld by the Company to satisfy tax withholding with respect to an award, and (iii) shares subject to a stock appreciation right that are not issued in connection with the stock settlement of the stock appreciation right on exercise. Shares of common stock under awards made in substitution or exchange for awards granted by a company acquired by the Company, or with which the Company combines, do not reduce the maximum number of shares that may be issued under the 2008 Plan. In addition, if a company acquired by the Company, or with which the Company combines, has shares remaining available under a plan approved by its stockholders, the available shares (adjusted to reflect the exchange or valuation ratio in the acquisition or combination) may be used for awards under the 2008 Plan and will not reduce the maximum number of shares of common stock that may be issued under the 2008 Plan; provided, however that awards using such available shares shall not be made after the date awards or grants could have been made under the pre-existing plan, absent the acquisition or combination, and shall only be made to individuals who were not our employees or directors prior to the acquisition or combination.

Under the 2008 Plan, the purchase price of shares of common stock covered by a stock option cannot be less than 100% of the fair market value of the common stock on the date the option is granted. Fair market value of the common stock is generally equal to the closing price for the common stock on the principal securities exchange on which the common stock is traded on the date the option is granted (or if there was no closing price on that date, on the last preceding date on which a closing price is reported). Option awards generally have ten-year

contractual terms and vest over four years based on continuous service; however, the 2005 Plan and the 2008 Plan allow for other vesting periods and we have granted employees options where the requisite service period is three years and we have granted our non-employee directors options where the requisite service period is three years, one year and, in one case, four months.

Table of Contents

ADVENTRX Pharmaceuticals, Inc. and Subsidiaries
(A Development Stage Enterprise)
Notes to Consolidated Financial Statements
December 31, 2010

We canceled options exercisable for 34,000 and 76,229 shares of common stock in the years ended December 31, 2010 and 2009, respectively, held by employees and directors whose service to our company terminated during those respective periods. The shares underlying such options were returned to and are available for re-issuance under the 2008 Plan pursuant to the terms described above.

During the year ended December 31, 2010, all awards granted under the 2008 Plan were stock options. During the year ended December 31, 2009, the awards granted under the 2008 Plan were stock options and restricted stock units. All the restricted stock units granted in the first quarter of 2009 were subsequently canceled in the first, second and third quarters of 2009. A summary of all of our option activity as of December 31, 2010 and 2009 and of changes in options outstanding under the plans during the year ended December 31, 2010 are as follows:

	Shares	Weighted-Average Exercise Price	Weighted-Average Remaining Contractual Years	Aggregate Intrinsic Value
Outstanding at December 31, 2009	234,356	$ 19.98		
Granted	203,381	$ 7.20		
Exercised				
Cancelled/forfeited/expired	(34,000)	$ 33.62		
Outstanding at December 31, 2010	403,737	$ 12.39	8.46	$ 19,600
Options exercisable at December 31, 2010	121,464	$ 26.88	7.56	$ 9,800
Vested and expected to vest at December 31, 2010	370,416	$ 12.91	8.42	$ 19,438

The weighted-average grant-date fair value of options granted during the years ended December 31, 2010 and 2009 was $6.91 and $3.18, respectively. As of December 31, 2010, there was approximately $1.1 million of unamortized compensation cost related to unvested stock option awards, which is expected to be recognized over a weighted-average period of approximately 2.5 years.

There were no options exercised during the years ended December 31, 2010 and 2009.

Our determination of fair value is affected by our stock price as well as a number of assumptions that require judgment. The fair value of each option award is estimated on the date of grant using the Black-Scholes option-valuation model. The assumptions used in the Black-Scholes option-valuation model for option grants to employees and non-employee directors during the years ended December 31, 2010 and 2009 are as follows:

	Years Ended December 31,	
	2010	2009
Risk-free interest rate	1.8 2.7%	2.7%
Dividend yield	0.0%	0.0%
Expected volatility	188 202%	183%
Expected term (in years)	5 6 years	6 years

Table of Contents

ADVENTRX Pharmaceuticals, Inc. and Subsidiaries
(A Development Stage Enterprise)
Notes to Consolidated Financial Statements
December 31, 2010

The risk-free interest rate assumption is based on the U.S. Treasury yield for a period consistent with the expected term of the option in effect at the time of the grant. We have not paid any dividends on common stock since our inception and do not anticipate paying dividends on our common stock in the foreseeable future. The expected option term is computed using the simplified method as permitted under the provisions of Staff Accounting Bulletin (SAB 107). SAB 107 s guidance was extended indefinitely by SAB 110. The expected volatility is based on the historical volatility of our common stock based on the daily close prices.

No options were granted to consultants in 2010 and 2009. We recognized $0 in share-based compensation expense associated with non-employee options in the years ended December 31, 2010 and 2009. In accordance with ASC 718, Compensation Stock Compensation, share-based compensation expense associated with the non-employee director options is included with employee share-based compensation expense.

The following table summarizes information concerning our outstanding and exercisable stock options as of December 31, 2010:

	Options Outstanding			Options Exercisable	
Range of Exercise Price	Number Outstanding	Weighted-Average Remaining Contractual Life	Weighted-Average Exercise Price	Number Exercisable	Weighted-Average Exercise Price
$1.63 to $3.25	155,998	8.67	$ 3.04	44,000	$ 2.88
$5.91 to $8.00	183,381	9.10	$ 7.79	22,888	$ 8.00
$9.25 to $13.50	28,000	6.92	$ 11.88	18,400	$ 11.03
$57.50 to $118.75	36,358	5.53	$ 76.04	36,176	$ 76.08
	403,737	8.46	$ 12.39	121,464	$ 26.88

Employee Stock Purchase Plan

The Purchase Plan was approved by our stockholders in 2005; however, we have not implemented the Purchase Plan. The Purchase Plan allows all eligible employees to purchase shares of common stock at 85% of the lower of the fair market value on the first or the last day of each offering period. Employees may authorize us to withhold up to 15% of their compensation during any offering period, subject to certain limitations. The maximum aggregate number of shares of common stock that may be issued under the Purchase Plan is 186,945 as of December 31, 2010. This maximum number is subject to an annual automatic increase on January 1 of each year equal to the lesser of (i) 1% of the number of outstanding shares of common stock on such day, (ii) 30,000 or (iii) such other amount as our board of directors may specify. At December 31, 2010, no shares of common stock have been issued under the Purchase Plan. On January 1, 2011, the number of shares of common stock available for issuance under the Purchase Plan increased by 30,000 in accordance with the provisions for annual increases under the Purchase Plan.

(8) Commitments

Operating Leases

We are obligated under operating leases for office space and equipment. In July 2004, we entered into a lease for office space in a facility in San Diego, California that served as our headquarters. In June 2005, we leased additional space in the same facility. During May 2009, the lease was extended for only a portion of the office space. The lease was set to expire in August 2009 and we vacated an additional portion of the facility at that time. During December 2009, we amended the lease to extend its term for an additional eight months through

January 31, 2011. During February 2010, we further amended the lease to lease adjacent office space through January 31, 2011, and to terminate our obligations with respect to the office space we were then occupying, effective March 1, 2010. During the year ended December 31, 2009, our average monthly office lease payment was $14,700 per month. During the year ended December 31, 2010, our average monthly office lease payment was $6,400 per month. We lease copiers and an automobile, which leases expire in 2015 and 2011, respectively.

Table of Contents

ADVENTRX Pharmaceuticals, Inc. and Subsidiaries
(A Development Stage Enterprise)
Notes to Consolidated Financial Statements
December 31, 2010

In December 2010, we entered into a new lease for office space at a different facility in San Diego, California to serve as our headquarters, effective January 1, 2011. The term of the new lease will expire January 31, 2012, unless we exercise our option to extend the lease an additional 12 months. The average base rent for this space is approximately $15,600 per month.

Rent expense was approximately $99,000 and $203,000 during the years ended December 31, 2010 and 2009, respectively.

Future rental commitments under all operating leases are as follows:

Year Ending December 31,	
2011	$ 205,562
2012	25,260
2013	8,326
2014	8,326
2015	694
Total	$ 248,168

(9) Licensing Revenue

In June 2010, we announced that we had entered into a license agreement with respect to our know-how to develop, make, use and sell ANX-510, or CoFactor® (5,10-methylenetetrahydrofolate), with Theragence, Inc., a California corporation (Theragence). Pursuant to the agreement, we granted to Theragence an exclusive worldwide license, including the right to grant sublicenses under certain circumstances, to conduct research on and to develop, make, have made, use, offer for sale, sell, have sold and import licensed products in any field or use. We are entitled to receive royalties on net sales of licensed products and commercial milestone payments of up to approximately $30 million based on aggregate gross sales of licensed products in the United States, European Union and Japan. Theragence agreed to use commercially reasonable efforts to research, develop and commercialize at least one licensed product. We discontinued active work on our CoFactor program in October 2008.

In March 2009, we announced that we and our wholly-owned subsidiary, SD Pharmaceuticals, Inc., had entered into a license agreement with respect to our product candidate ANX-514 (docetaxel emulsion for injection) with Shin Poong Pharmaceutical Co., Ltd., a company organized under the laws of the Republic of Korea (Shin Poong), pursuant to which we granted to Shin Poong an exclusive license, including the right to sublicense, to research, develop, make, have made, use, offer for sale, sell and import licensed products, in each case solely for the treatment of cancer by intravenous administration of formulations of docetaxel as emulsified products and solely in South Korea. Under the terms of the agreement, we received an upfront licensing fee of $0.3 million, and are entitled to receive a regulatory milestone payment of either $0.2 million or $0.4 million upon receipt of regulatory approval for marketing a licensed product in South Korea (the amount depends on whether the Korea Food and Drug Administration requires Shin Poong to conduct a bioequivalence or clinical study in human subjects prior to receipt of regulatory approval), one-time commercial milestone payments tied to annual net sales of licensed products in an aggregate amount of up to $1.5 million and royalty payments on net sales of licensed products. Shin Poong is responsible for all development and commercial activities related to ANX-514 in South Korea. We agreed to pay Shin Poong $0.1 million if the Korea Food and Drug Administration required Shin Poong to conduct a bioequivalence or clinical trial in human subjects prior to receipt of regulatory approval and we elect not to supply product to conduct such trial, which supply obligation is subject to limitations.

Table of Contents

ADVENTRX Pharmaceuticals, Inc. and Subsidiaries
(A Development Stage Enterprise)
Notes to Consolidated Financial Statements
December 31, 2010

We received the $0.3 million upfront licensing fee in April 2009. We recognized $0.3 million in licensing revenue in the three-month period ended March 31, 2009 because the criteria under our revenue recognition policy were met in that period.

In September 2010, pursuant to the terms of the license agreement, we elected to make the $0.1 million cash payment to Shin Poong in lieu of supplying product for the ANX-514 trial in human subjects required by the Korea Food and Drug Administration.

(10) Grant Revenue

In November 2010, the Internal Revenue Service notified us that an aggregate amount of $488,959 in grants had been awarded to us under the qualifying therapeutic discovery project (QTDP) program established under Section 48D of the Internal Revenue Code as a result of the Patient Protection and Affordable Care Act of 2010. We submitted applications in July 2010 for qualified investments we made, or expected to make, in 2009 and 2010 in our ANX-530, or Exelbine , and ANX-514 programs, and a grant in the amount of $244,479 was approved for each of those programs. These grants are not taxable for federal income tax purposes. We received full payment of the grants in November 2010, all of which we recognized as revenue in the three month period ended December 31, 2010 because the criteria under our revenue recognition policy were met in that period.

(11) Income Taxes

Due to our historical net loss position, and as we have recorded a full valuation allowance against net deferred tax assets, there is no provision or benefit for income taxes recorded for the years ended December 31, 2010 and 2009.

The income tax provision/(benefit) is different from that which would be obtained by applying the statutory Federal income tax rate of 34% to income before income tax expense. The items causing this difference for the years ended December 31, 2010 and 2009 are as follows:

	December 31,	
	2010	**2009**
Income tax benefit at federal statutory rate	$ (2,873,000)	$ (3,851,000)
R & D credit	1,625,000	(150,000)
Stock options	164,000	770,000
Net operating true-ups	26,574,000	(20,000)
Other	(163,000)	62,000
Change in federal valuation allowance	(25,327,000)	3,189,000
Total	$	$

Table of Contents

ADVENTRX Pharmaceuticals, Inc. and Subsidiaries
(A Development Stage Enterprise)
Notes to Consolidated Financial Statements
December 31, 2010

Deferred income taxes reflect the net tax effect of temporary differences between the carrying amount of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. Significant components of deferred tax assets and liabilities at December 31, 2010 and 2009 are as follows:

	December 31, 2010	December 31, 2009
Deferred tax assets:		
Accrued expenses	$ 57,252	$ 85,538
Stock options expense under ASC 718	1,129,227	1,008,517
Net operating loss carry forwards	12,732,504	37,484,836
Income tax credit carry forwards	202,215	2,478,625
Property and equipment	6,820	12,094
Intangibles	2,246,349	2,360,396
Other	6,108	6,553
Total deferred tax assets	16,380,475	43,436,559
Less: valuation allowance	(16,380,475)	(43,436,559)
Total deferred tax assets, net of valuation allowance	$	$

We have established a full valuation allowance against our net deferred tax assets due to the uncertainty surrounding the realization of such assets. Management has determined it is more likely than not that the deferred tax assets are not realizable due to our historical loss position.

The deferred tax asset for net operating losses and the related valuation allowance includes approximately $47,000 related to stock option deductions, the benefit of which may eventually be credited to equity. We recognize windfall tax benefits associated with the exercise of stock options directly to stockholders equity only when realized. Accordingly, as we are in a cumulative loss position, deferred tax assets have not been recognized for net operating loss carry forwards resulting from windfall tax benefits generated through stock option deductions.

At December 31, 2010, we had federal and California tax loss carry forwards of approximately $31.5 million and $34.4 million, respectively. The federal and California net operating loss carry forwards begin to expire in 2016 and 2013, respectively, if unused. At December 31, 2010, we had federal and California R&D tax credit carry forwards of approximately $145,000 and $87,000, respectively. The federal R&D tax credits will begin to expire in 2029. The California R&D tax credits do not expire.

Pursuant to the Internal Revenue Code of 1986, as amended, (IRC) §382 and IRC §383, our ability to use net operating loss and R&D tax credit carry forwards to offset future taxable income is limited if we experience a cumulative change in ownership of more than 50% within a three-year period. During 2010, we completed a formal study for the period January 1, 2008 through January 7, 2010. This study and a previous study identified several ownership changes within the meaning of IRC §382. Upon application of limitations prescribed by IRC §382, we identified certain tax attributes that would expire before utilization and have adjusted our deferred tax assets for net operating loss and R&D tax credit carry forwards accordingly. We will need to update the IRC §382 analysis since January 7, 2010 for the subsequent registered direct equity financing completed during the year ended December 31, 2010. If an ownership change occurred after January 7, 2010, including as a result of the equity financings we completed in May 2010 and January 2011, the amount of net operating loss and R&D

tax credit carry forwards available for utilization would be subject to further limitation.

In accordance with authoritative guidance, the impact of an uncertain income tax position on the income tax return must be recognized at the largest amount that is more-likely-than-not to be sustained upon audit by the relevant taxing authority. An uncertain income tax position will not be recognized if it has less than a 50% likelihood of being sustained. As of December 31, 2010, we continue to have no unrecognized tax benefits. There are no unrecognized tax benefits included on the balance sheet that would, if recognized, impact the effective tax rate. We do not anticipate there will be a significant change in unrecognized tax benefits within the next 12 months.

Our policy is to recognize interest and/or penalties related to income tax matters in income tax expense. Because we have generated net operating losses since inception, no tax liability, penalties or interest has been recognized for balance sheet or income statement purposes as of and for the years ended December 31, 2010 and 2009.

Table of Contents

ADVENTRX Pharmaceuticals, Inc. and Subsidiaries
(A Development Stage Enterprise)
Notes to Consolidated Financial Statements
December 31, 2010

We are subject to taxation in the U.S. and the state of California. All of our tax years are subject to examination by the tax authorities due to the carry forward of unutilized net operating losses and R&D tax credits.

(12) Litigation

In the normal course of business, we may become subject to lawsuits and other claims and proceedings. Such matters are subject to uncertainty and outcomes are often not predictable with assurance. We are not currently a party to any material pending litigation or other material legal proceeding.

(13) 401(k) Plan

We have a defined contribution savings plan pursuant to Section 401(k) of the IRC. The plan is for the benefit of all qualifying employees and permits voluntary contributions by employees up to 100% of eligible compensation, subject to the Internal Revenue Service (IRS)-imposed maximum limits. From January 1, 2008 until May 16, 2009, the terms of the plan required us to make matching contributions equal to 100% of employee contributions up to 6% of eligible compensation, limited by the IRS-imposed maximum. In April 2009, we amended the plan such that we were not required to make matching contributions on any employee contributions made by a highly-compensated employee from May 16, 2009 through December 31, 2009. In November 2009, we amended the plan to reinstate the 6% matching contribution effective for the plan year beginning January 1, 2010. We incurred total expenses of $47,250 and $29,661 in employer matching contributions in 2010 and 2009, respectively.

(14) Segment Information

We operate our business on the basis of a single reportable segment, which, fundamentally, is the business of acquiring, developing and commercializing proprietary product candidates. We evaluate our Company as a single operating segment. The majority of our operating activities and work performed by our employees are currently conducted from a single location in the U.S. We recognized revenues of $0.5 million and $0.3 million in 2010 and 2009, respectively, which revenues were derived from U.S. government grants in 2010 and license fees under a license agreement with Shin Poong Pharmaceutical Co., Ltd. in 2009.

(15) Summary of Quarterly Financial Data (unaudited)

The following is a summary of the unaudited quarterly results of operations for the years ended December 31, 2010 and 2009:

Quarterly statements of operations data

	Quarters Ended			
for 2010 (unaudited):	**March 31**	**June 30**	**September 30**	**December 31**
Grant revenue	$	$	$	$ 488,959
Gross margin				488,959
Loss from operations	(2,419,885)	(1,942,750)	(1,868,138)	(2,308,924)
Net loss	(2,403,074)	(1,919,442)	(1,843,899)	(2,284,507)
Net loss applicable to common stock	(4,917,994)	(5,044,318)	(1,843,899)	(2,284,507)
Basic and diluted net loss per share	$ (0.48)	$ (0.39)	$ (0.13)	$ (0.15)
Basic and diluted weighted average number of shares of common stock outstanding	10,143,789	12,886,826	14,701,216	14,921,292

Table of Contents

ADVENTRX Pharmaceuticals, Inc. and Subsidiaries
(A Development Stage Enterprise)
Notes to Consolidated Financial Statements
December 31, 2010

	Quarters Ended			
for 2009 (unaudited):	**March 31**	**June 30**	**September 30**	**December 31**
Licensing revenue	$ 300,000	$	$	$
Gross margin	300,000			
Loss from operations	(3,158,786)	(2,552,485)	(2,349,865)	(3,224,549)
Net loss	(3,157,010)	(2,595,541)	(2,352,586)	(3,219,921)
Net loss applicable to common stock	(3,157,010)	(3,827,956)	(2,728,675)	(6,478,304)
Basic and diluted net loss per share	$ (0.87)	$ (1.02)	$ (0.57)	$ (1.00)
Basic and diluted weighted average number of shares of common stock outstanding	3,610,102	3,735,572	4,779,228	6,509,266

(16) Severance Related Expenses

As part of restructuring to reduce operating costs, we completed workforce reductions of nine employees in the three months ended December 31, 2008 and fifteen employees in the six months ended June 30, 2009. As a result, we recorded severance-related charges of $350,000 in the first quarter of 2009, of which $237,000 was recorded in research and development and the balance was recorded in selling, general and administrative, and $163,000 in the second quarter of 2009, of which $121,000 was recorded in research and development and the balance was recorded in selling, general and administrative. As of June 30, 2009, all severance-related costs associated with these workforce reductions had been recorded and paid. No severance-related costs were recorded or paid during the year ended December 31, 2010.

(17) Subsequent Events

On January 11, 2011, we completed a registered direct equity financing involving the issuance of units consisting of 8,184,556 shares of our common stock, 5-year warrants to purchase up to an aggregate of 2,046,139 shares of our common stock and 1-year warrants to purchase up to an aggregate of 2,046,139 shares of our common stock. The gross proceeds of this financing were $22.5 million, and we received $21.0 million in net proceeds after deducting the fees and expenses of our placement agent and our other offering expenses. We may receive up to $11.3 million of additional proceeds from the exercise of the warrants issued in this financing. Those warrants have an exercise price of $2.75 per share. The 5-year warrants are exercisable any time on or before January 11, 2016 and the 1-year warrants are exercisable any time on or before January 19, 2012, subject to certain beneficial ownership limitations.

In November 2010, we submitted a new drug application (NDA), for Exelbine to the U.S. Food and Drug Administration (FDA), and in January 2011, we announced that the FDA accepted the Exelbine NDA for filing and established a Prescription Drug User Fee Act, or PDUFA, goal date of September 1, 2011 to finish its review of the Exelbine NDA.

Table of Contents

ADVENTRX Pharmaceuticals, Inc. and Subsidiaries
(A Development Stage Enterprise)
Notes to Consolidated Financial Statements
December 31, 2010

In February 2011, we entered into an agreement and plan of merger to acquire SynthRx, Inc. (SynthRx), a privately-held Delaware corporation developing a purified form of a rheologic and antithrombotic agent, poloxamer 188 (188), in exchange for shares of our common stock. As discussed in more detail under Part I, Item 1 Business in this report, we initially intend to develop purified 188 for the treatment of sickle cell crisis in a pediatric population and, if our acquisition of SynthRx closes and we are able to reach agreement with the FDA on a study protocol on a timely basis, we may initiate a phase 3 clinical trial of purified 188 for that indication in 2012. In connection with the consummation of this acquisition, we would issue 2,938,773 shares of our common stock to SynthRx s stakeholders, 1,938,773 of which would be subject to repurchase by us in the event development of purified 188 does not achieve the first milestone described below. We could issue up to an aggregate of 13,478,050 additional shares of our common stock to SynthRx s stakeholders if the development of purified 188 achieves certain milestones, as described below, and our stockholders approve the issuance of such milestone-related shares, as required by NYSE Amex rules. If our stockholders do not approve the issuance of the milestone-related shares, under the terms of the merger agreement, we would be required to pay SynthRx s stakeholders in cash the value of the milestone-related shares we would have otherwise issued, with all such cash payments made in quarterly installments and, with respect to the cash value associated with 12,478,050 of the milestone-related shares, payable based on net sales of purified 188. Of the shares issuable in connection with achievement of milestones, up to 1,000,000 shares would be issuable upon the dosing of the first patient in a phase 3 clinical study that the FDA has indicated may be sufficient to support approval of a new drug application covering the use of purified 188 for the treatment of sickle cell crisis in children (the 188 NDA), which we refer to as the first milestone; 3,839,400 shares would be issuable upon acceptance for review of the 188 NDA by the FDA, which we refer to as the second milestone; and 8,638,650 shares would be issuable upon approval by the FDA of the 188 NDA, which we refer to as the third milestone.

Table of Contents

Exhibit Index

Exhibit	Description
2.1(1)	Agreement and Plan of Merger, dated April 7, 2006, among the registrant, Speed Acquisition, Inc., SD Pharmaceuticals, Inc. and certain individuals named therein (including exhibits thereto)
3.1(2)	Amended and Restated Certificate of Incorporation of the registrant
3.2(3)	Certificate of Amendment to the Amended and Restated Certificate of Incorporation of the registrant dated October 5, 2009
3.3(4)	Certificate of Amendment to the Amended and Restated Certificate of Incorporation of the registrant, dated April 23, 2010
3.4(5)	Certificate of Designation of Preferences, Rights and Limitations of 0% Series A Convertible Preferred Stock
3.5(6)	Certificate of Designation of Preferences, Rights and Limitations of 5% Series B Convertible Preferred Stock
3.6(7)	Certificate of Designation of Preferences, Rights and Limitations of 5% Series C Convertible Preferred Stock
3.7(8)	Certificate of Designation of Preferences, Rights and Limitations of 4.25660% Series D Convertible Preferred Stock
3.8(9)	Certificate of Designation of Preferences, Rights and Limitations of 3.73344597664961% Series E Convertible Preferred Stock
3.9(10)	Certificate of Designation of Preferences, Rights and Limitations of 2.19446320054018% Series F Convertible Preferred Stock
3.10(11)	Amended and Restated Bylaws of the registrant (formerly known as Biokeys Pharmaceuticals, Inc.)
10.1(12)	Securities Purchase Agreement, dated July 21, 2005, among the registrant and the Purchasers (as defined therein)
10.2(12)	Rights Agreement, dated July 27, 2005, among the registrant, the Icahn Purchasers and Viking (each as defined therein)
10.3(13)	First Amendment to Rights Agreement, dated September 22, 2006, among the registrant and the Icahn Purchasers (as defined therein)
10.4(14)	Second Amendment to Rights Agreement, dated February 25, 2008, among the registrant and the Icahn Purchasers (as defined therein)
10.5(15)	

	Third Amendment to Rights Agreement, dated August 26, 2009, among the registrant and Icahn Purchasers (as defined therein)
10.6(12)	Form of $2.26 Common Stock Warrant issued on July 27, 2005 to Icahn Partners LP, Icahn Partners Master Fund LP, High River Limited Partnership, Viking Global Equities LP and VGE III Portfolio Ltd.
10.7(12)	Form of $2.26 Common Stock Warrant issued on July 27, 2005 to North Sound Legacy Institutional Fund LLC and North Sound Legacy International Ltd.
10.8(5)	Engagement Letter Agreement, dated June 7, 2009, by and between the registrant and Rodman & Renshaw, LLC
10.9(5)	Securities Purchase Agreement, date June 8, 2009, governing the issuance and sale of the registrant s 0% Series A Convertible Preferred Stock and 5-year common stock purchase warrants

Table of Contents

Exhibit	Description
10.10(5)	Form of Common Stock Purchase Warrant issued on June 12, 2009 by the registrant to the purchasers of the registrant s 0% Series A Convertible Preferred Stock and to Rodman & Renshaw, LLC
10.11(6)	Engagement Letter Agreement, dated June 26, 2009, by and between the registrant and Rodman & Renshaw, LLC
10.12(6)	Securities Purchase Agreement, dated June 29, 2009, governing the issuance and sale of the registrant s 5% Series B Convertible Preferred Stock
10.13(6)	Form of Common Stock Purchase Warrant issued on July 6, 2009 by the registrant to Rodman & Renshaw, LLC
10.14(7)	Engagement Letter Agreement, dated August 4, 2009, by and between the registrant and Rodman & Renshaw, LLC
10.15(7)	Securities Purchase Agreement, dated August 5, 2009, governing the issuance and sale of the registrant s 5% Series C Convertible Preferred Stock
10.16(7)	Form of Common Stock Purchase Warrant issued on August 10, 2009 by the registrant to Rodman & Renshaw, LLC
10.17(16)	Engagement Letter Agreement, dated September 24, 2009, by and between the registrant and Rodman & Renshaw, LLC
10.18(8)	Engagement Letter Agreement, dated September 29, 2009, by and between the registrant and Rodman & Renshaw, LLC
10.19(8)	Form of Securities Purchase Agreement, dated October 6, 2009, governing the issuance and sale of the registrant s 4.25660% Series D Convertible Preferred Stock and 5-year common stock purchase warrants
10.20(8)	Form of Common Stock Purchase Warrant issued on October 9, 2009 by the registrant to the purchasers of the registrant s 4.25660% Series D Convertible Preferred Stock and to Rodman & Renshaw, LLC
10.21(9)	Engagement Letter Agreement, dated January 3, 2010, by and between the registrant and Rodman & Renshaw, LLC
10.22(9)	Securities Purchase Agreement, dated as of January 4, 2010, governing the issuance and sale of the registrant s 3.73344597664961% Series E Convertible Preferred Stock and 30-month common stock purchase warrants
10.23(9)	Form of Common Stock Purchase Warrant issued on January 7, 2010 by the registrant to the purchasers of the registrant s 3.73344597664961% Series E Convertible Preferred Stock and to Rodman & Renshaw, LLC

10.24(10)	Engagement Letter Agreement, dated April 29, 2010, by and between the registrant and Rodman & Renshaw, LLC
10.25(10)	Form of Securities Purchase Agreement, dated May 2, 2010 governing the issuance and sale of the registrant s 2.19446320054018% Series F Convertible Preferred Stock and 5-year and 1-year common stock purchase warrants
10.26(10)	Form of Series A and B Common Stock Purchase Warrants issued on May 6, 2010 by the registrant to the purchasers of the registrant s 2.19446320054018% Series F Convertible Preferred Stock
10.27(17)	Engagement Letter Agreement, dated January 5, 2011, by and between the registrant and Rodman & Renshaw, LLC

Table of Contents

Exhibit	Description
10.28(17)	Form of Securities Purchase Agreement, dated January 6, 2011 governing the issuance and sale of the registrant s common stock and 5-year and 1-year common stock purchase warrants
10.29(17)	Form of [Series A/B] Common Stock Purchase Warrant issued on January 11, 2011 by the registrant to the purchasers of the registrant s common stock and to Rodman & Renshaw, LLC
10.30#(18)	2005 Equity Incentive Plan
10.31#(19)	Form of Stock Option Agreement under the 2005 Equity Incentive Plan
10.32#(20)	Form of Stock Option Agreement under the 2005 Equity Incentive Plan (for director option grants beginning in 2008)
10.33#(21)	Form of Stock Option Agreement under the 2005 Equity Incentive Plan (for option grants to employees approved in March 2008)
10.34#(2)	Form of Restricted Share Award Agreement under the 2005 Equity Incentive Plan
10.35#(22)	2008 Omnibus Incentive Plan
10.36#(23)	Form of Notice of Grant of Restricted Stock Units under the 2008 Omnibus Incentive Plan (for grants to employees in January 2009)
10.37#(23)	Form of Restricted Stock Units Agreement under the 2008 Omnibus Incentive Plan
10.38#(24)	Form of Non-Statutory Stock Option Grant Agreement (for directors) under the 2008 Omnibus Incentive Plan
10.39#(24)	Form of Non-Statutory/Incentive Stock Option Grant Agreement (for consultants/employees) under the 2008 Omnibus Incentive Plan
10.40#(25)	Form of Incentive Stock Option Grant Agreement under the 2008 Omnibus Incentive Plan (for grant to Brian M. Culley in July 2009)
10.41#(25)	Form of Incentive Stock Option Grant Agreement under the 2008 Omnibus Incentive Plan (for grant to Patrick L. Keran in July 2009)
10.42#(26)	Form of letter, dated January 20, 2010, modifying options granted to Brian M. Culley and Patrick L. Keran in July 2009
10.43#(26)	Form of Incentive Stock Option Grant Agreement under the 2008 Omnibus Incentive Plan (for grant to Brian M. Culley in January 2010)
10.44#(26)	Form of Incentive Stock Option Grant Agreement under the 2008 Omnibus Incentive Plan (for grant to Patrick L. Keran in January 2010)

10.45(20)	License Agreement, dated December 10, 2005, among SD Pharmaceuticals, Latitude Pharmaceuticals and Andrew Chen, including a certain letter, dated November 20, 2007, clarifying the scope of rights thereunder
10.46 (27)	License Agreement, dated March 25, 2009, among the registrant, SD Pharmaceuticals, Inc. and Shin Poong Pharmaceutical Co., Ltd.
10.47(28)	Standard Multi-Tenant Office Lease Gross, dated June 3, 2004, between the registrant and George V. Casey & Ellen M. Casey, Trustees of the Casey Family Trust dated June 22, 1998
10.48(2)	First Amendment to the Standard Multi-Tenant Office Lease Gross, dated June 3, 2004 between the registrant and George V. & Ellen M. Casey, Trustees of the Casey Family Trust dated June 22, 1998
10.49(29)	Second Amendment to Standard Mutli-Tenant Office Lease Gross, dated July 22, 2009, by and among Westcore Mesa View, LLC, DD Mesa View LLC and the registrant

Table of Contents

Exhibit	Description
10.50(30)	Third Amendment to Standard Multi-Tenant Office Lease Gross, dated December 10, 2009, by and among Westcore Mesa View, LLC, DD Mesa View, LLC and the registrant
10.51(31)	Fourth Amendment to Standard Multi-Tenant Office Lease Gross, dated February 4, 2010, by and among Westcore Mesa View, LLC, DD Mesa View, LLC and the registrant
10.52#(32)	Offer letter, dated November 15, 2004, to Brian M. Culley
10.53#(23)	Retention and Incentive Agreement, dated January 28, 2009 between the registrant and Brian M. Culley
10.54#(27)	Retention and Incentive Agreement, dated January 28, 2009, between the registrant and Patrick L. Keran
10.55#(31)	Consulting Agreement, effective as of July 15, 2009, and Amendment to Consulting Agreement, effective as of December 31, 2009, between the registrant and Michele L. Yelmene
10.56#(25)	2009 Mid-Year Incentive Plan for Brian M. Culley and Patrick L. Keran
10.57#(25)	Retention and Severance Plan (as of July 21, 2009) for Brian M. Culley and Patrick L. Keran
10.58#(26)	2010 Incentive Plan for Brian M. Culley and Patrick L. Keran
10.59#(31)	Consulting Agreement, effective as of November 23, 2009, between the registrant and Eric K. Rowinsky
10.60#(33)	Director Compensation Policy, adopted June 21, 2006
10.61#(31)	Director Compensation Policy, adopted January 25, 2010
10.62(34)	Form of Director and Officer Indemnification Agreement
21.1	List of Subsidiaries
23.1	Consent of J.H. Cohn LLP, Independent Registered Public Accounting Firm
31.1	Certification of principal executive officer pursuant to Rule 13a-14(a)/15d-14(a)
31.2	Certification of principal financial officer pursuant to Rule 13a-14(a)/15d-14(a)
32.1±	Certification of principal executive officer and principal financial officer pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

Indicates that confidential treatment has been requested or granted to certain portions, which portions have been omitted and filed separately with the SEC

# Indicates management contract or compensatory plan

± These certifications are being furnished solely to accompany this report pursuant to 18 U.S.C. 1350, and are not being filed for purposes of Section 18 of the Securities Exchange Act of 1934 and are not to be incorporated by reference into any filing of the registrant, whether made before or after the date hereof, regardless of any general incorporation by reference language in such filing.

(1) Filed with the registrant s Amendment No. 1 to Current Report on Form 8-K/A on May 1, 2006 (SEC file number 001-32157-06796248)

(2) Filed with the registrant s Annual Report on Form 10-K on March 16, 2006 (SEC file number 001-32157-06693266)

(3) Filed with the registrant s Current Report on Form 8-K on October 13, 2009 (SEC file number 001-32157-091115090)

Table of Contents

(4) Filed with the registrant s Current Report on Form 8-K on April 26, 2010 (SEC file number 001-32157-10769058)

(5) Filed with the registrant s Current Report on Form 8-K on June 8, 2009 (SEC file number 001-32157-09878961)

(6) Filed with the registrant s Current Report on Form 8-K on June 30, 2009 (SEC file number 001-32157-09917820)

(7) Filed with the registrant s Current Report on Form 8-K on August 5, 2009 (SEC file number 001-32157-09989205)

(8) Filed with the registrant s Amendment No. 3 to the Registration Statement on Form S-1 on October 5, 2009 (SEC file number 333-160778-091107945)

(9) Filed with the registrant s Current Report on Form 8-K on January 4, 2010 (SEC file number 001-32157-10500379)

(10) Filed with the registrant s Current Report on Form 8-K on May 3, 2010 (SEC file number 001-32157-10790486)

(11) Filed with the registrant s Current Report on Form 8-K on December 15, 2008 (SEC file number 001-32157-081249921)

(12) Filed with the registrant s Quarterly Report on Form 10-Q on August 12, 2005 (SEC file number 001-32157-051022046)

(13) Filed with the registrant s Current Report on Form 8-K on September 22, 2006 (SEC file number 001-32157-061103268)

(14) Filed with the registrant s Current Report on Form 8-K on February 25, 2008 (SEC file number 001-32157 08638638)

(15) Filed with the registrant s Current Report on Form 8-K on September 1, 2009 (SEC file number 001-32157-091049161)

(16) Filed with the registrant s Amendment No. 2 to the Registration Statement on Form S-1 on September 25, 2009 (SEC file number 333-160778-091087750)

(17) Filed with the registrant s Current Report on Form 8-K on January 7, 2011 (SEC file number 001-32157-11515655)

(18) Filed with the registrant s Annual Report on Form 10-K on March 15, 2007 (SEC file number 001-32157-07697283)

(19) Filed with the registrant s Registration Statement on Form S-8 on July 13, 2005 (SEC file number 333-126551-05951362)

(20) Filed with registrant s Annual Report on Form 10-K on March 17, 2008 (SEC file number 001-32157-08690952)

(21) Filed with the registrant s Quarterly Report on Form 10-Q on May 12, 2008 (SEC file number 001-32157-08820541)

(22) Filed with the registrant s Current Report on Form 8-K on June 2, 2008 (SEC file number 001-32157-08874724)

(23) Filed with the registrant s Current Report on Form 8-K on February 2, 2009 (SEC file number 001-32157-09561715)

(24) Filed with the registrant s Quarterly Report on Form 10-Q on August 11, 2008 (SEC file number 001-32157-081005744)

(25) Filed with the registrant s Current Report on Form 8-K on July 22, 2009 (SEC file number 001-32157-09957353)

(26) Filed with the registrant s Current Report on Form 8-K on January 26, 2010 (SEC file number 001-32157-10547818)

Table of Contents

(27) Filed with the registrant s Quarterly Report on Form 10-Q on May 15, 2009 (SEC file number 001-32157-09878961)

(28) Filed with the registrant s Quarterly Report on Form 10-QSB on August 10, 2004 (SEC file number 001-32157-04963741)

(29) Filed with the registrant s Current Report on Form 8-K on August 20, 2009 (SEC file number 001-32157-091025631)

(30) Filed with the registrant s Current Report on Form 8-K on December 24, 2009 (SEC file number 001-32157-091260100)

(31) Filed with the registrant s Annual Report on Form 10-K on March 18, 2010 (SEC file number 001-32157-10692317)

(32) Filed with the registrant s Annual Report on Form 10-KSB on March 31, 2005 (SEC file number 001-32157-05719975)

(33) Filed with the registrant s Current Report on Form 8-K on June 23, 2006 (SEC file number 001-32157-06922676)

(34) Filed with the registrant s Current Report on Form 8-K on October 23, 2006 (SEC file number 001-32157-061156993)