

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D. C. 20549

FORM 8-K

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

DATE OF REPORT (DATE OF EARLIEST EVENT REPORTED): MARCH 29, 2000

HALSEY DRUG CO., INC.

695 NO. PERRYVILLE ROAD, ROCKFORD, ILLINOIS

(815)-399-2060

Incorporated under the laws of
State of New YorkCommission File Number
1-10113I.R.S. Employer Identification Number
11-0853640

ITEM 2. DISPOSITION OF ASSETS

On March 29, 2000, Halsey Drug Co., Inc. (the "Company" or "Halsey") completed various strategic alliance transactions with Watson Pharmaceuticals, Inc. ("Watson"). The transactions with Watson provided for Watson's purchase of a certain pending ANDA from the Company, for Watson's rights to negotiate for Halsey to manufacture and supply certain identified future products to be developed by Halsey and for Watson's extension of a \$17,500,000 term loan to the Company. Reference is made to "Item 5. Other Events" below for a description of Watson's negotiation rights for certain future products and the \$17,500,000 term loan to the Company.

The product acquisition portion of the transactions with Watson provided for Halsey's sale of a pending ANDA and related regulatory approval and intellectual property rights (collectively, the "Product") to Watson for aggregate consideration of \$13,500,000. The amount of the purchase price, the amount included in each installment and the timing of payment of the installments were determined in arms-length negotiations between the parties. As part of the execution of the Product acquisition agreement, the Company and Watson executed ten year supply agreements covering the active pharmaceutical ingredient ("API") and finished dosage form of the Product pursuant to which Halsey, at Watson's discretion, will manufacture and supply Watson's requirements for the Product API and, where the Product API is sourced from the Company, finish dosage forms of the Product. The purchase price for the Product is payable in three approximately equal installments as certain milestones are achieved. Prior to the Product purchase transaction and the transactions described in "Item 5. Other Events" below, there was no relationship or business dealings between the Company and Watson.

ITEM 5. OTHER EVENTS

In connection with the closing of the sale of the Product by the Company to Watson as described in Item 2 above, the Company and Watson executed a right of first negotiation agreement providing Watson with a first right to negotiate the terms under which the Company would manufacture and supply certain specified APIs and finished dosage products to be developed by the Company. The right of first negotiation agreement provides that upon Watson's exercise of its right to negotiate for the supply of a particular product, the parties will negotiate the specific terms of the manufacturing and supply arrangement, including price, minimum purchase requirements, if any, territory and term. In the event Watson does not exercise its right of first negotiation upon receipt of written notice from the Company as to its receipt of applicable governmental approval relating to a covered product, or in the event the parties are unable to reach agreement on the material terms of a supply arrangement relating to such product within sixty (60) days of Watson's exercise of its right to negotiate for such product, the Company may negotiate with third parties for the supply, marketing and sale of the applicable product. The right of first negotiation agreement has a term of ten years, subject to extension in the absence of written notice from either party for two additional periods of five years each. The right of first negotiation agreement applies only to API and finished dosage products identified in the agreement and does not otherwise prohibit the Company from developing APIs or finished dosage products for itself or third parties.

The Company and Watson also executed a manufacturing and supply agreement providing for Watson's marketing and sale of the Company's existing core products portfolio (the "Core Products Supply Agreement"). The Core Products Supply Agreement obligates Watson to purchase a minimum amount of approximately \$18,363,000 (the "Minimum Purchase Amount") in core products from the Company, in equal quarterly installments over a period of 18 months (the "Minimum Purchase Period"). At the expiration of the Minimum Purchase Period, if Watson does not continue to satisfy the Minimum Purchase Amount the Company may market and sell the core products on its own or through a third party. Pending the Company's development and receipt of regulatory approval for its APIs and finished dosage products currently under development, and the marketing and sale of same, of which there can be no assurance, substantially all the Company's revenues will be derived from the Core Products Supply Agreement with Watson.

The final component of the Company's strategic alliance with Watson provided for Watson's extension of a \$17,500,000 term loan to the Company. The loan will be funded in installments upon the Company's request for advances and the provision to Watson of a supporting use of proceeds relating to each such installment. The loan is secured by a first lien on all of the Company's assets, senior to the lien securing all other Company indebtedness, carries a floating rate of interest equal to prime plus two percent and matures on March 31, 2003. The net proceeds from the term loan will, in large part, be used to upgrade and equip the API manufacturing facility of Houba, Inc., the Company's wholly-owned subsidiary, to upgrade and equip the Company's Congers, New York leased facility, to satisfy approximately \$3,300,000 in bridge financing provided by Galen Partners and for working capital to fund continued operations.

ITEM 7. FINANCIAL STATEMENTS, PRO FORMA FINANCIAL INFORMATION AND EXHIBITS.

(c) Exhibits

Exhibit No. -----	Description -----
10.57	Loan Agreement dated March 29, 2000 between the Registrant and Watson Pharmaceuticals, Inc.*
10.58	Amendment to Loan Agreement dated March 31, 2000 between the Registrant and Watson Pharmaceuticals, Inc.
10.59	Secured Promissory Note in the principal amount of \$17,500,000 issued by the Registrant, as the maker, in favor of Watson Pharmaceuticals, Inc. dated March 31, 2000.
10.60	Watson Security Agreement dated March 29, 2000 between the Registrant and Watson Pharmaceuticals, Inc.

- 10.61 Stock Pledge Agreement dated March 29, 2000 between the Registrant and Watson Pharmaceuticals, Inc.
- 10.62 Watson Guarantee dated March 29, 2000 between Houba, Inc. and Watson Pharmaceuticals, Inc., as the guarantors, in favor of Watson Pharmaceuticals, Inc.
- 10.63 Watson's Guarantors Security Agreement dated March 29, 2000 between Halsey Pharmaceuticals, Inc., Houba, Inc. and Watson Pharmaceuticals, Inc.
- 10.64 Subordination Agreement dated March 29, 2000 by and among the Registrant, Watson Pharmaceuticals, Inc. and the holders of the Registrant's outstanding 5% convertible debentures due March 10, 2003.
- 10.65 Real Estate Mortgage dated March 29, 2000 between Houba, Inc. and Watson Pharmaceuticals, Inc.
- 10.66 Subordination Agreement by and among Houba, Inc., Galen Partners, III, L.P., Oracle Strategic Partners, L.P. and Watson Pharmaceuticals, Inc.
- 10.67 Product Purchase Agreement dated March 29, 2000 between the Registrant and Watson Pharmaceuticals, Inc.*
- 10.68 Finished Goods Supply Agreement dated March 29, 2000 between the Registrant and Watson Pharmaceuticals, Inc.*
- 10.69 Active Ingredient Supply Agreement dated March 29, 2000 between the Registrant and Watson Pharmaceuticals, Inc.*
- 10.70 Right of First Negotiation Agreement dated March 29, 2000 between the Registrant and Watson Pharmaceuticals, Inc.*
- 10.71 Finished Goods Supply Agreement (Core Products) dated March 29, 2000 between the Registrant and Watson Pharmaceuticals, Inc. *

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 * A portion of this exhibit has been omitted pursuant to an application for confidential treatment filed with the Securities and Exchange Commission pursuant to Rule 24b-2 of Securities Exchange Act of 1934, as amended.

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.

HALSEY DRUG CO., INC.

By:\s\ Michael Reicher

Michael Reicher
President and Chief Executive Officer

Date: April 12, 2000

EXHIBIT INDEX

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LOAN AGREEMENT

This LOAN AGREEMENT, dated as of March 29, 2000 (the "Loan Agreement"), is made and entered into by and between Halsey Drug Co., Inc., a New York corporation ("Borrower"), and Watson Pharmaceuticals, Inc., a Nevada corporation ("Lender"). Capitalized terms used herein shall have the meanings given them in Section 12.1 below.

RECITALS

WHEREAS, concurrently herewith, the Lender and the Borrower are entering into, among other agreements, that certain Product Purchase Agreement (the "Purchase Agreement"), pursuant to which Lender will purchase from Borrower its [] product (the "Product") and related assets; those certain Supply Agreements (the "Supply Agreements"), pursuant to which Borrower will supply Lender with the finished Product and the active pharmaceutical ingredient for the Product, respectively; and that Right of First Negotiation Agreement (the "Negotiation Agreement"), pursuant to which Lender have a right to negotiate supply agreements with Borrower for other pharmaceutical compounds or finished goods with respect to which Borrower has or may acquire manufacturing rights;

WHEREAS, in order to develop its business and perform its obligations under the Product Agreements, Borrower will require additional access to credit;

WHEREAS, it is therefore a condition to the execution of the Purchase Agreement and the Supply Agreements that Lender loan to Borrower the principal amount of Seventeen Million Five Hundred Thousand Dollars (\$17,500,000) on the terms and conditions set forth herein;

WHEREAS, pursuant to that certain Debenture and Warrant Purchase Agreement, dated as of March 10, 1998 (the "1998 Debenture Agreement"), executed by Borrower in favor of the Purchasers named therein, Borrower issued its 5% Convertible Senior Secured Debentures Due March 15, 2003 (such debentures, the "Galen Debentures");

WHEREAS, pursuant to that certain Debenture and Warrant Purchase Agreement, dated May 26, 1999 (the "1999 Debenture Agreement"), executed by Borrower in favor of the Purchasers named therein, Borrower issued its 5% Convertible Senior Secured Debentures Due March 15, 2003 (such debentures, the "Oracle Debentures," and collectively with the Galen Debentures, the "Existing Debentures"). The holders of the Galen Debentures and the Oracle Debentures as of a given date are sometimes referred to herein as the "Existing Holders."

WHEREAS, to induce Lender to make the Loan, (i) Borrower will grant to Lender a first priority perfected security interest in its assets; (ii) the Borrower's subsidiaries will execute guaranties in favor of Lender, guaranteeing the Borrower's obligations hereunder, and security agreements in support of such guaranties, naming Lender a secured party; and (iii) Houba, Inc., a wholly-owned subsidiary of the Borrower, shall execute a mortgage on certain real property in Culver, Indiana in favor of Lender; and

WHEREAS, as further inducement for the Lender to make the Loan, Lender, the holders of the Galen Debentures, the holders of the Oracle Debentures, Borrower and certain of the Guarantors will enter into that certain Subordination Agreement, dated as of even date herewith and substantially in the form attached hereto as Exhibit A (the "Subordination Agreement"), pursuant to which the

parties thereto shall agree that Lender shall be entitled to satisfaction in full of Borrower's obligations under this Loan Agreement prior to the satisfaction of Borrower's obligations under the Existing Debentures (exclusive of interest payment obligations, subject to the terms of the Subordination Agreement);

NOW, THEREFORE, in consideration of the foregoing recitals and the covenants herein contained, the parties hereto agree as follows.

AGREEMENT

1. AMOUNT AND TERMS OF LOAN.

1.1 Term Loan. Subject to the terms herein, Lender agrees to loan to Borrower the principal amount of Seventeen Million Five Hundred Thousand Dollars (\$17,500,000) (the "Loan"). Only one such Loan shall be made hereunder, notwithstanding any prepayment of the Loan by Borrower, and sums repaid hereunder may not be re-borrowed.

1.2 Promissory Note. Borrower's obligation to pay the principal of, and interest on, the Loan shall be evidenced by a secured promissory note in the form attached hereto as Exhibit B (the "Note"), duly executed and delivered by Borrower.

2. SECURITY FOR THE LOAN; GUARANTIES.

2.1 Collateral. All of the obligations of Borrower under this Loan Agreement shall be secured by (a) a first priority lien on all the personal property and assets of Borrower, now existing or hereinafter acquired, granted to the Lender pursuant to a security agreement substantially in the form attached hereto as Exhibit C (the "Watson Security Agreement"), which, except for Permitted Liens, shall be a first priority lien and senior in priority to the liens in favor of the Existing Holders, (b) collateral assignments substantially in the form attached hereto as Exhibit D (the "Watson Collateral Assignments"), executed by the Borrower in favor of the Lender; and (c) a stock pledge agreement substantially in the form attached hereto as Exhibit E (the "Watson Stock Pledge Agreement"), executed by Borrower in favor of Lender, pledging all of the capital stock of the Guarantors to the Lender in support of the Obligations.

2.2 Guaranties. All of the Obligations of Borrower shall be guaranteed pursuant to a guaranty substantially in the form attached hereto as Exhibit F (the "Watson Guaranty"), executed by the Guarantors in favor of the Lender.

2.3 Guarantor Security Documents. All of the obligations of the Guarantors under the Guaranties shall be secured by (a) a lien on all of the personal property and assets of the respective Guarantors, now existing or hereinafter acquired, granted to the Lender pursuant to a security agreement substantially in the form attached hereto as Exhibit G (the "Watson Guarantors Security Agreement"), which, except for Permitted Liens, shall be first liens and senior in priority to the Guarantors' liens in favor of the Existing Holders; (b) collateral assignments substantially in the form attached hereto as Exhibit H (the "Watson Guarantors Collateral Assignments"), executed by the Guarantors in favor of the Lender; and (c) a first mortgage covering Houba's Culver, Indiana real property (the "Watson Mortgage").

The Watson Security Agreement, the Watson Collateral Assignment, the Watson Stock Pledge Agreement, the Watson Guaranty, the Watson Guarantors Security Agreement, the Watson Guarantor Collateral Assignments and the Watson Mortgage are sometimes referred to collectively herein as the "Watson Security Documents." The Loan Agreement, the Note, the Watson Security Documents and the Subordination Agreement are sometimes referred to collectively herein as the "Loan Documents."

3. CLOSING. The closing of this Loan Agreement (the "Closing") will take place at the offices of Stradling Yocca Carlson & Rauth at 660 Newport Center Drive, Suite 1600, Newport Beach, California 92660, simultaneously with the execution of this Loan Agreement, or such other place, time and date as shall be mutually agreed to by Lender and Borrower. Such time and date is herein called the "Closing Date."

4. CONDITIONS PRECEDENT. The obligation of Lender to make the Loan is subject to the satisfaction of the following conditions.

4.1 Execution of Note. Borrower shall have executed and delivered to Lender the Note.

4.2 Execution of Subordination Agreement. Borrower shall have executed and delivered to Lender, and shall have caused the other parties thereto (except Lender) to have executed and delivered, the Subordination Agreement.

4.3 Execution of Related Agreements. Borrower shall have executed and delivered to Lender the Purchase Agreement, the Supply Agreements and the Negotiation Agreement.

4.4 Amended Brooklyn Facility Lease. Borrower shall have executed and delivered, and shall have caused the lessor under the Brooklyn Facility Lease to have executed and delivered, an amendment to the Brooklyn Facility Lease in form and substance reasonably acceptable to the Lender.

4.5 No Default; Representations and Warranties. At the time of making the Loan and also after giving effect thereto: (a) there shall have occurred no Event of Default (as defined in Section 8.1 below), and (b) all representations and warranties contained in the Loan Documents shall be true and correct in all material respects.

4.6 Corporate Documents; Proceedings. All corporate and legal proceedings and all instruments and agreements in connection with the transactions contemplated in the Loan Documents shall be satisfactory in form and substance to Lender, and Lender shall have received all information and copies of all documents and papers, including records of corporate proceedings and governmental approvals, if any, which Lender reasonably may have requested in connection therewith, such documents and papers to be certified where appropriate by proper corporate or governmental authorities.

4.7 Watson Security Documents. Borrower shall have duly authorized, executed and delivered, and/or shall have caused the Agent, the holders of the Oracle Debentures and the Guarantors, as applicable, to have duly authorized, executed and delivered, the Watson Security Documents, together with:

(a) copies of duly authorized, executed and proper UCC-1 Financing Statements, in a form suitable for filing under the UCC of each jurisdiction as may be necessary or, in the reasonable opinion of Lender, desirable to perfect the security interests purported to be created by the Watson Security Documents (the "Financing Statements"), such Financing Statements to be filed, or to be caused to be filed, as soon as practicable, but in no event later than ten Business Days, following the Closing;

(b) certified copies of UCC-11 Requests for Information or equivalent reports, listing all other effective financing statements that name Borrower as debtor and that are filed in the jurisdictions referred to in clause (a) above, together with copies of such other financing statements (none of which shall cover the Collateral except those issued in connection with the Existing Debentures or to the extent evidencing Permitted Liens);

(c) copies of such other duly authorized, executed and proper recordings and filings, including filings in the U.S. Patent and Trademark Office, as may be necessary or, in the opinion of Lender, desirable to perfect the security interests purported to be created by the Watson Security Documents;

(d) copies of such duly authorized, executed and proper recordings and filings as may be necessary or, in the opinion of Lender, desirable to evidence the Watson Mortgage in the applicable state, county and local recorders office;

(e) [intentionally omitted]; and

(f) evidence that all other actions necessary or, in the opinion of Lender, desirable to perfect and protect the security interests purported to be created by the Watson Security Documents have been or will be taken.

4.8 Consents. Borrower shall have obtained all necessary consents or waivers, if any, from all parties to any other material agreements to which Borrower is a party or by which it is bound immediately prior to the Closing in order that the transactions contemplated hereby may be consummated and the business of Borrower may be conducted by Borrower after the Closing without adversely affecting Borrower, including, without limitation, (a) the consent of the Agent and the holders of the Oracle Debentures to the execution of the Loan Documents and the transactions contemplated thereby; and (b) the consents of the holders of the Existing Debentures required pursuant to Section 6.2 with respect to non-cash interest payments.

4.9 Other Deliveries. Borrower shall have delivered to Lender:

(a) a copy of the Certificate of Incorporation of Borrower and each Guarantor and all amendments thereto, certified by the Secretary of State for the jurisdiction of incorporation of each;

(b) a copy of the By-Laws of Borrower and each Guarantor as amended to date, certified as being true and complete by a principal officer of Borrower;

(c) a Certificate of Good Standing and Tax Status from the state of incorporation of Borrower and each Guarantor and from every state in which any of them is qualified to do business; and

(d) true and complete copies of the mortgages and all material transaction documents (including, without limitation, the disclosure schedules thereto) pertaining to the issuance of the Galen Debentures and the Oracle Debentures, certified as such by a principal officer of Borrower.

4.10 Due Diligence Investigation. No fact shall have been discovered which in Lender's sole determination would make the consummation of the transactions contemplated by this Loan Agreement not in Lender's best interests.

4.11 Opinion of Counsel. Lender shall have received the opinion of St. John & Wayne, L.L.C., counsel to Borrower, dated the Closing Date, substantially in the form of Exhibit I attached hereto.

5. REPRESENTATIONS AND WARRANTIES OF BORROWER. The Borrower represents and warrants as follows:

5.1 Organization and Existence, etc. Except as set forth in Section 5.1 of the Schedule of Exceptions attached hereto (the "Schedule of Exceptions"), or in the Borrower's Annual Report on Form 10-K for the fiscal year ended December 31, 1998, as amended, or the Borrower's Quarterly Report on Form 10-Q for the quarter ended September 30, 1999 (collectively, the "Selected Reports"), (a) the Borrower is a corporation duly organized and validly existing and in good standing under the laws of its jurisdiction of incorporation, and has all requisite corporate power and authority to carry on its business as now conducted and proposed to be conducted; (b) the Borrower has all requisite corporate power and authority to enter into this Loan Agreement and to carry out and perform its obligations under the terms and conditions of this Loan Agreement. Except as set forth in Section 5.1 of the Schedule of Exceptions, the Borrower does not own or lease any property or engage in any activity in any jurisdiction which might require qualification to do business as a foreign corporation in such jurisdiction and where the failure to so qualify would have a material adverse effect on the financial condition of the Borrower and its Subsidiaries, taken as a whole, or subject the Borrower to a material liability. To the extent the Borrower has not qualified to do business in such jurisdictions, it will prepare and file such necessary applications or documents to be filed with the appropriate authorities in such jurisdictions to obtain such qualifications within 60 days. The Borrower has furnished the Lender with true, correct and complete copies of its Certificate of Incorporation, By-Laws and all amendments thereto to date.

5.2 Subsidiaries and Affiliates. Section 5.2 of the Schedule of Exceptions sets forth the name, jurisdiction of incorporation and authorized and outstanding capitalization of each entity in which the Borrower owns securities having a majority of the voting power in the election of directors or persons serving equivalent functions (each, a "Subsidiary"). Except as set forth in Section 5.2 of the Schedule of Exceptions, the Borrower has, and upon the Closing will have, no Subsidiaries and does not, and upon the Closing will not, own of record or beneficially any capital stock or equity interest or investment in any corporation, association or business entity. Except as set forth in Section 5.2 of the Schedule of Exceptions or in the Selected Reports, each Subsidiary is a corporation duly organized and validly existing and in good standing under the laws of its jurisdiction of incorporation and has all requisite corporate power and authority to carry on its business as now conducted and proposed to be conducted. Except as set forth in Section 5.2 of the Schedule of Exceptions, no Subsidiary owns or leases any property or engages in any activity in any jurisdiction which might require such Subsidiary to qualify to do business as a foreign corporation in such jurisdiction and where the failure to so qualify would have a material adverse effect on the financial

condition of the Borrower and its Subsidiaries, taken as a whole, or subject such Subsidiary to a material liability. To the extent any Subsidiary has not qualified to do business in such jurisdictions, it will prepare and file such necessary applications or documents to be filed with the appropriate authorities in such jurisdictions to obtain such qualifications within 60 days. None of Cenci Power Products, Inc., a Delaware corporation, H.R. Cenci Laboratories, Inc., a California corporation, Blue Cross Products, Inc., a New York corporation, and Indiana Fine Chemicals, Inc., a Delaware corporation, each wholly-owned Subsidiaries of Borrower (the "Immaterial Subsidiaries"), have any material assets or conduct any material business operation.

5.3 Capitalization.

(a) As of the date hereof, the Borrower's authorized capital stock consists of 80,000,000 shares of Common Stock, par value \$.01 per share, of which 14,439,622 shares are outstanding and 47,888,808 of which are reserved for issuance for the purposes set forth in Section 5.3 of the Schedule of Exceptions, 31,889,792 of which have been reserved for issuance upon conversion of the Existing Debentures and 10,258,716 of which have been reserved for issuance upon exercise of the Warrants. As of the date hereof, the Borrower holds 439,603 shares of Common Stock in its treasury which shares may be reissued.

(b) All the issued and outstanding shares of capital stock of the Borrower shall, as of the Closing, (i) have been duly authorized and validly issued, (ii) be fully paid and nonassessable and (iii) have been offered, issued, sold and delivered by the Borrower in compliance with applicable federal and state securities laws. Other than as set forth in Section 5.3 of the Schedule of Exceptions or the Selected Reports, there are no outstanding preemptive, conversion or other rights, options, warrants, calls, agreements or commitments granted or issued by or binding upon the Borrower, for the purchase or acquisition of any shares of its capital stock or securities convertible into or exercisable or exchangeable for capital stock.

5.4 Authorization. All corporate action on the part of the Borrower and the directors and stockholders of the Borrower necessary for the authorization, execution, delivery and performance by the Borrower of this Loan Agreement and the transactions contemplated herein has been taken or will have been taken prior to the Closing.

5.5 Binding Obligations; No Material Adverse Contracts, etc. The Loan Agreement is a valid and binding obligation of the Borrower enforceable in accordance with its terms. Except as set forth in Section 5.5 of the Schedule of Exceptions, the execution, delivery and performance by the Borrower of this Loan Agreement and compliance herewith will not result in any violation of and will not conflict with, or result in a breach of any of the terms of, or constitute a default under, any provision of state or federal law to which the Borrower is subject, the Certificate of Incorporation, as amended, or the By-Laws, as amended, of the Borrower, or any mortgage, indenture, agreement, instrument, judgment, decree, order, rule or regulation or other restriction to which the Borrower is a party or by which it is bound, or except for liens on the assets of the Borrower created in favor of the Lender, result in the creation of any mortgage, pledge, lien, encumbrance or charge upon any of the properties or assets of the Borrower pursuant to any such term.

5.6 Compliance with Instruments, etc. Except as set forth in Section 5.6 of the Schedule of Exceptions or the Selected Reports, neither the Borrower nor any Subsidiary is (a) in default past any grace, notice or cure period under any indenture, agreement or instrument to which it is a party or by which it is bound, (b) in violation of its Certificate of Incorporation, By-Laws or of any

applicable law, (c) in default with respect to any order, writ, injunction or decree of any court, administrative agency or arbitrator, or (d) in default under any order, license, regulation or demand of any government agency, which default or violation would materially and adversely affect the business, properties or condition (financial or otherwise) of the Borrower and its Subsidiaries taken as a whole.

5.7 Litigation. Except as set forth in Section 5.7 of the Schedule of Exceptions or the Selected Reports, there is no action, suit or proceeding pending, or, to the knowledge of the Borrower, threatened, against the Borrower or any Subsidiary before any court, administrative agency or arbitrator or any action, suit or proceeding pending, or, to the knowledge of the Borrower, threatened, which challenges the validity of any action taken or to be taken pursuant to or in connection with this Loan Agreement.

5.8 Financial Information; SEC Documents.

(a) Borrower has furnished to Lender the consolidated financial statements of Borrower and its Subsidiaries, including consolidated balance sheets as of December 31, 1998 and 1997 and consolidated statements of operations, changes in cash flows and stockholders' equity, covering the three years ended December 31, 1998, all of which statements have been certified by Grant Thornton LLP, certified public accountants, and all of which statements are included or incorporated by reference in Borrower's Annual Report on Form 10-K for the year ended December 31, 1998 filed with the Commission under the Exchange Act. Such financial statements fairly present the condition of Borrower and its Subsidiaries as of the dates thereof and the results of the operations of Borrower and its Subsidiaries for such periods.

(b) Borrower has also furnished to Lender the unaudited consolidated balance sheets of Borrower and its Subsidiaries as of December 31, 1999, and the related unaudited consolidated statements of operations, consolidated statements of cash flow and consolidated statements of stockholders' equity for the three months and twelve months ended December 31, 1999 and December 31, 1998. Such financial statements fairly present, in conformity with United States generally accepted accounting principles ("GAAP") applied on a basis consistent with the financial statements referred to in paragraph (a) of this section, the consolidated financial position of Borrower and its Subsidiaries as of such date and their consolidated results of operations for such periods (subject to normal year-end adjustments). Since December 31, 1999, Borrower has not had net losses (as calculated in conformity with GAAP applied on a basis consistent with the financial statements referred to in paragraph (a) of this section) of more than \$5,000,000.

(c) None of the documents filed by the Borrower with the Commission since June 30, 1998 contain any untrue statement of a material fact or omit to state a material fact required to be stated therein or necessary in order to make the statements contained therein not false or misleading in light of the circumstances in which they were made. There is no fact known to the Borrower which the Borrower has not disclosed to the Lender prior to or as of the date of this Loan Agreement which materially and adversely affects, or in the future is likely to materially and adversely affect, the business, properties, condition (financial or otherwise) or business prospects of the Borrower and its Subsidiaries, taken as a whole.

5.9 Permits; Governmental and Other Approvals.

(a) Other than as set forth in Section 5.9 of the Schedule of Exceptions or the Selected Reports, each of the Borrower and its Subsidiaries possesses such franchises, licenses, permits and other authority as are necessary for the conduct of its business as now being conducted and proposed to be conducted (except where the failure to possess such franchises, licenses, permits or other authority would not materially and adversely affect the business, properties or condition (financial or otherwise) of the Borrower and its Subsidiaries taken as a whole) and the Borrower and its Subsidiaries are not in default under any of such franchises, licenses, permits or other authority. Other than as set forth in Section 5.9 of the Schedule of Exceptions or the Selected Reports, no approval, consent, authorization or other order of, and no designation, filing, registration, qualification or recording with, any governmental authority or any other person or entity is required in connection with the Borrower's valid execution, delivery and performance of this Loan Agreement or the consummation of any other transaction contemplated on the part of the Borrower hereby.

(b) Without limiting the generality of the representations and warranties made in Section 5.9, the Borrower represents and warrants that (i) it and its Subsidiaries are in compliance in all material respects with all applicable provisions of the Federal Food, Drug, and Cosmetic Act (the "FDC Act"), (ii) its products and those of its Subsidiaries are not adulterated or misbranded and are in lawful distribution, and (iii) it and its Subsidiaries are in compliance with the following specific requirements: the Borrower and its Subsidiaries have registered all facilities with the United States Food and Drug Administration (the "FDA"); the Borrower and its Subsidiaries have listed all drug products with the FDA; each drug product marketed by the Borrower or any Subsidiary is the subject of an application approved by the FDA; all marketed drug products comply with any conditions of approval and the terms of the application submitted to the FDA; all drug products are manufactured in compliance with the FDA's good manufacturing practice regulations; all products are labeled and promoted in accordance with the terms of the marketing application and the provisions of the FDC Act; all adverse events that were required to be reported to the FDA have been reported to the FDA in a timely manner; each of the Borrower and its Subsidiaries is in compliance in all material respects with the terms of the consent agreement entered into by the Borrower with the United States Attorney for the Eastern District of New York on behalf of the FDA on June 29, 1993, as amended to date; to the Borrower's knowledge, neither the Borrower nor any Subsidiary is employing or utilizing the services of any individual who has been debarred under the FDC Act; all stability studies required to be performed for products distributed by the Borrower or a Subsidiary have been completed or are ongoing in accordance with the applicable FDA requirements; any products exported by the Borrower or a Subsidiary have been exported in compliance with the FDC Act; and each of the Borrower and its Subsidiaries is in compliance in all material respects with the provisions of the Federal Food, Drug, and Cosmetic Act, to the extent applicable.

(c) Without limiting the generality of the representations and warranties made in Section 5.9(a), the Borrower also represents and warrants that it and its Subsidiaries are in compliance in all material respects with all applicable provisions of the Controlled Substances Act (the "CSA") and that the Borrower and its Subsidiaries are in compliance with the following specific requirements: the Borrower and its Subsidiaries are registered with the Drug Enforcement Administration (the "DEA") at each facility where controlled substances are exported, imported, manufactured or distributed; all controlled substances are stored and handled pursuant to DEA security requirements; all records and inventories of receipt and distributions of controlled substances are maintained in the manner and form as required by DEA regulations; all reports, including, but not limited to, ARCOS, manufacturing quotas, production quotas, and disposals, have been submitted to DEA in a timely manner; all adverse events, including thefts or significant losses of controlled substances, have been reported to DEA in a timely manner; to the Borrower's knowledge, neither the

Borrower nor any Subsidiary is employing any individual, with access to controlled substances, who has previously been convicted of a felony involving controlled substances; and any imports or exports of controlled substances have been conducted in compliance with the CSA and DEA regulations.

5.10 Sales Representatives, Customers and Key Employees. Other than as set forth in Section 5.10 of the Schedule of Exceptions or the Selected Reports, to the knowledge of the Borrower, no independent sales representatives, customers or key employees or group of key employees of the Borrower or its Subsidiaries has any intention to terminate his, her or its relationship with the Borrower or such Subsidiary on or after the Closing or in the case of employees, leave, as of the Closing, the employ of the Borrower on and after the Closing. Other than as set forth in Section 5.10 of the Schedule of Exceptions or the Selected Reports or as contemplated by this Agreement, all personnel are employed on an "at will" basis and may be terminated upon notice of not more than 30 days.

5.11 Copyrights, Trademarks and Patents.

(a) Section 5.11 of the Schedule of Exceptions sets forth a list of all of the Borrower's and any Subsidiary's patents, patent applications, trademarks, copyrights, trademark registrations and applications therefor, patent, trademark or trade name licenses, contracts with employees or others relating in whole or in part to disclosure, assignment or patenting of any inventions, discoveries, improvements, processes, formulae or other know-how, and all patent, trademark or trade names or copyright licenses which are in force (referred to collectively as "Intellectual Property Rights"). The Intellectual Property Rights are, to the best of the Borrower's knowledge and belief, fully valid and are in full force and effect.

(b) The Borrower or a Subsidiary owns outright all of the Intellectual Property Rights listed on Section 5.11 of the Schedule of Exceptions attached hereto and, except as set forth in Section 8.3(1), such Intellectual Property is free and clear of all liens and encumbrances and neither Borrower nor its Subsidiaries pay any royalty to anyone under or with respect to any of them.

(c) Neither the Borrower nor any Subsidiary has licensed anyone to use any of such Intellectual Property Rights and has no knowledge of the infringing use by the Borrower or any Subsidiary of any intellectual property rights.

(d) The Borrower has no knowledge, nor has it received any notice (i) of any conflict with the asserted rights of others with respect to any Intellectual Property Rights used in, or useful to, the operation of the business conducted by the Borrower and its Subsidiaries or with respect to any license under which the Borrower or a Subsidiary is licensor or licensee; or (ii) that the Intellectual Property Rights infringe upon the rights of any third party.

5.12 Inventory. All inventory of the Borrower consists of a quality and quantity usable and salable in the ordinary course of business, except for obsolete items and items of below-standard quality, all of which have been or will be written off or written down to net realizable value on the unaudited consolidated balance sheet of the Borrower and its Subsidiaries as of December 31, 1999. The quantities of each type of inventory (whether raw materials, work-in-process, or finished goods) are not excessive, but are reasonable and warranted in the present circumstances of the Borrower.

5.13 No Discrimination. Neither the Borrower nor any Subsidiary in any manner or form discriminates, fosters discrimination or permits discrimination against any person belonging to any minority race or believing in any minority creed or religion.

5.14 Environmental Matters.

(a) Each of the Borrower and its Subsidiaries has obtained all environmental, health and safety permits necessary or required for the operation of its business (except where the failure to possess such franchises, licenses, permits or other authority would not materially and adversely affect the business, properties or condition (financial or otherwise) of the Borrower and its Subsidiaries taken as a whole), and all such permits are in full force and effect and each of the Borrower and its Subsidiaries is in compliance in all material respects with all terms and conditions of such permits.

(b) Except as set forth in Section 5.14 of the Schedule of Exceptions or the Selected Reports, there is no proceeding pending or, to the best knowledge of the Borrower, threatened, which may result in the denial, rescission, termination, modification or suspension of any environmental or health or safety permits necessary for the operation of the business of the Borrower and its Subsidiaries.

(c) Except as set forth in Section 5.14 of the Schedule of Exceptions or the Selected Reports, during the occupancy by the Borrower or any Subsidiary of any real property leased by the Borrower or such Subsidiary, and to the best knowledge of the Borrower, no other person or entity, has caused or permitted materials to be generated, released, stored, treated, recycled, disposed of on, under or at such parcels, which materials, if known to be present, would require clean up, removal or other remedial or responsive action under any Environmental Law. To the best knowledge of the Borrower, there are no underground storage tanks and no polychlorinated biphenyls ("PCB's"), PCB contaminated oil or asbestos on any property leased by the Borrower or any Subsidiary.

(d) Except as set forth in Section 5.14 of the Schedule of Exceptions or the Selected Reports, neither the Borrower nor any Subsidiary is subject to any judgment, decree, order or citation related to or arising out of Environmental Laws, or has received notice that it has been named or listed as a potentially responsible party by any person or governmental body or agency in any matter arising under Environmental Laws.

(e) To the best of knowledge of the Borrower, each of the Borrower and its Subsidiaries has disposed of all waste in full compliance with all Environmental Laws.

5.15 Taxes. Except as set forth in Section 5.15 of the Schedule of Exceptions or the Selected Reports, the Borrower and each of its Subsidiaries have filed all necessary income, franchise and other material tax returns, domestic and foreign and have paid all taxes shown as due thereunder, and the Borrower has no knowledge of any tax deficiency which might be assessed against the Borrower or any of the Subsidiaries which, if so assessed, would have a material adverse effect on the business, properties, assets, net worth, condition (financial or other), or results of operations of the Borrower and its Subsidiaries taken as a whole.

5.16 Employee Benefit Plans and Similar Arrangements.

(a) Section 5.16 of the Schedule of Exceptions lists all employee benefit plans and collective bargaining, labor and employment agreements or other similar arrangements in effect to which the Borrower, its Subsidiaries, and any of its ERISA Affiliates are a party or by which the Borrower, its Subsidiaries, and any of its ERISA Affiliates are bound, legally or otherwise, including, without limitation, any profit-sharing, deferred compensation, bonus, stock option, stock purchase, pension, retainer, consulting, retirement, severance, welfare or incentive plan, agreement or arrangement; any plan, agreement or arrangement providing for fringe benefits or perquisites to employees, officers, directors or agents, including but not limited to benefits relating to employer-supplied automobiles, clubs, medical, dental, hospitalization, life insurance and other types of insurance, retiree medical, retiree life insurance and any other type of benefits for retired and terminated employees; any employment agreement; or any other "employee benefit plan" (within the meaning of Section 3(3) of the Employee Retirement Income Security Act of 1974, as amended through the date of this Agreement ("ERISA")) (herein referred to individually as "Plan" and collectively as "Plans"). For purposes of this Agreement, "ERISA Affiliate" means (i) any corporation which at any time on or before the Closing Date is or was a member of the same controlled group of corporations (within the meaning of Section 414(b) of the Code as the Borrower, its Subsidiaries, or any ERISA Affiliate; (ii) any partnership, trade or business (whether or not incorporated) which at any time on or before the Closing Date is or was under common control (within meaning of Section 414(c) of the Code) with the Borrower, its Subsidiaries, or any ERISA Affiliate; and (iii) any entity which at any time on or before the Closing Date is or was a member of the same affiliated service group (within the meaning of Section 414(m) of the Code) as the Borrower, its Subsidiaries or any ERISA Affiliate, or any corporation described in clause (i) or any partnership, trade or business described in clause (ii) of this paragraph.

(b) True and complete copies of the following documents with respect to any Plan of the Borrower, its Subsidiaries, and each ERISA Affiliate, as applicable, have been delivered to the Lender: (i) the most recent Plan document and trust agreement (including any amendments thereto and prior plan documents, if amended with the last two years), (ii) the last two Form 5500 filings and schedules thereto, (iii) the most recent IRS determination letter, (iv) all summary plan descriptions, (v) a written description of each material non-written Plan, (vi) each written communication to employees intended to describe a Plan or any benefit provided by such Plan, (vii) the most recent actuarial report, and (viii) all correspondence with the IRS, the Department of Labor and the Pension Benefit Guaranty Corporation concerning any controversy. Each report described in clause (vii) accurately reflects the funding status of the Plan to which it relates and subsequent to the date of such report there has been no adverse change in the funding status or financial condition of such Plan.

(c) Each Plan is and has been maintained in compliance in all material respects with applicable law, including but not limited to ERISA, and the Code and with any applicable collective bargaining agreements or other contractual obligations.

(d) Except as shown on Section 5.16 of the Schedule of Exceptions, with respect to any Plan that is subject to Section 412 of the Code ("412 Plan"), there has been no failure to make any contribution or pay any amount due as required by Section 412 of the Code, Section 302 of ERISA or the terms of any such Plan, and no funding waiver has been requested or received from the IRS. The assets of the Borrower, its Subsidiaries, or and ERISA Affiliates are not now, nor will they after the passage of time be, subject to any lien imposed under Code Section 412(n) by reason of a failure of the Borrower, any Subsidiary, or any ERISA Affiliate to make timely installments or other payments required under Code Section 412.

(e) Except as shown on Section 5.16 of the Schedule of Exceptions or in the Selected Reports, no Plan subject to Title IV of ERISA has any "Unfunded Pension Liability." For purpose of this Agreement, Unfunded Pension Liability means, as of any determination date, the amount, if any, by which the present value of all benefit liabilities (as that term is defined in Section 4001(a)(16) of ERISA) of a plan subject to Title IV of ERISA exceeds the fair market value of all assets of such plan, all determined using the actuarial assumptions that would be used by the PBGC in the event of a termination of the plan on such determination date.

(f) Except as shown on Section 5.16 of the Schedule of Exceptions, to the best knowledge of the Borrower, its Subsidiaries, and ERISA Affiliates, there are no pending or threatened claims, actions or lawsuits, other than routine claims for benefits in the ordinary course, asserted or instituted against (i) any Plan or its assets, (ii) any ERISA Affiliate with respect to any 412 Plan, or (iii) any fiduciary with respect to any Plan for which the Borrower, its Subsidiaries, or any ERISA Affiliate may be directly or indirectly liable, through indemnification obligations or otherwise.

(g) Neither the Borrower, any Subsidiary, nor any ERISA Affiliate has incurred and or reasonably expects to incur (i) any withdrawal liabilities as defined in Section 4201 of ERISA ("Withdrawal Liability") and no event has occurred which, with the giving of notice under Section 4219 of ERISA, would result in Withdrawal Liabilities, or any liability under Section 4063, 4064, or 4243, or (ii) any outstanding liability under Title IV of ERISA with respect to any 412 Plan.

(h) (h) Except as shown on Section 5.16 of the Schedule of Exceptions, within the last five years, neither the Borrower, any Subsidiary, nor any ERISA Affiliate has transferred any assets or liabilities of a 412 Plan subject to Title IV of ERISA which had, at the date of such transfer, an Unfunded Pension Liability or has engaged in a transaction which may reasonably be subject to Section 4212(c) or Section 4069 of ERISA.

(i) Neither the Borrower, any Subsidiary, nor any ERISA Affiliate has engaged, directly or indirectly, in a non-exempt prohibited transaction (as defined in Section 4975 of the Code or Section 406 of ERISA) in connection with any Plan.

(j) Except as shown on Section 5.16 of the Schedule of Exceptions, neither the Borrower, any Subsidiary, nor any ERISA Affiliate has any unfunded liability with respect to any non-tax qualified deferred compensation plan.

(k) The Lender will not have (i) an obligation to make contribution(s) to any multiemployer plan (as defined in Section 3(37) of ERISA), or (ii) any Withdrawal Liability (whether imposed and not yet paid or calculated assuming a complete or partial withdrawal of the Borrower, any Subsidiary, or any ERISA Affiliate as of such date not yet imposed) which it would not have had it not entered into the transactions described in this Agreement.

(l) Except as shown on Section 5.16 of the Schedule of Exceptions, during the last two years there have been no amendments to any Plan, no written interpretation or announcement (whether or not written) by the Borrower, any Subsidiary, or any ERISA Affiliate relating to any Plan, there have been and are no negotiations, demands, or proposals which are pending that concern any Plan, nor has any Plan been established, which resulted in or could result in a material increase in (i) the accrued or promised benefits of any employees of the Borrower, or any

Subsidiary, or any ERISA Affiliate and (ii) any material increase in the level of expense incurred in respect thereof.

(m) There has been no "Reportable Event" with respect to any 412 Plan subject to Title IV of ERISA within the last five years.

(n) Neither the Borrower, any Subsidiary, nor any ERISA Affiliate sponsors, maintains or has obligations, direct, contingent or otherwise, with respect to any Plan that is subject to the laws of any country other than the United States.

(o) No ERISA Affiliate maintains an employee stock ownership plan or other plan holding securities of the Borrower, any Subsidiary, or any ERISA Affiliate.

(p) Each Plan that provides welfare benefits has been operated in compliance with all requirements of Sections 601 through 608 of ERISA and either (i) Section 162(i)(2) and (k) of the Code and regulations thereunder (prior to 1989) or (ii) Section 4980B of the Code and regulations thereunder after 1988, relating to the continuation of coverage under certain circumstances in which coverage would otherwise cease. Neither the Borrower, any Subsidiary, nor any ERISA Affiliate has contributed to a nonconforming group health plan (as defined under Code Section 5000(c) and no ERISA Affiliate has incurred a tax under Section 5000(a) of the Code which could become a liability of the Borrower, any Subsidiary, or any ERISA Affiliate. Except as shown on Section 5.16 of the Schedule of Exceptions or in the Selected Reports, the Borrower, any Subsidiary, or any ERISA Affiliate does not and has not maintained, sponsored or provided post-retirement medical benefits, post-retirement death benefits or other post-retirement welfare benefits to its current employees or former employees except as required by Section 4980B of the Code and at the sole expense of the participant or the beneficiary of the participant. The Borrower has complied in all respects with all requirements of the Health Insurance Portability and Accountability Act of 1996 with respect to each Plan that provides welfare benefits.

(q) Except as shown on Section 5.16 of the Schedule of Exceptions, the Borrower, its Subsidiaries, and its ERISA Affiliates has funded or will fund each Plan in accordance with the terms of such Plan through the Closing Date, including the payment of applicable premiums on any insurance contract funding a Plan, for coverage provided through the Closing Date.

(r) No Plan has been amended since the date of its most recent IRS determination letter which would materially increase its cost and no Plan has been amended in a manner that would require security to be provided in accordance with Section 401(a)(29) of the Code.

(s) Each Plan that is intended to be a tax qualified Plan under Section 401(a) of the Code ("Tax Qualified Plan") has been determined by the IRS to qualify under Section 401 of the Code, and the trusts created thereunder have been determined to be exempt from tax under the provisions of Section 501 of the Code, and to the best knowledge of the Borrower, its Subsidiaries, and its ERISA Affiliates nothing has occurred, including the adoption of or failure to adopt any Plan amendment, which would adversely affect its qualification or tax-exempt status.

(t) Except as disclosed on Section 5.16 of the Schedule of Exceptions, no employee or former employee of the Borrower, any Subsidiary, or any ERISA Affiliate will become entitled to any bonus, retirement, severance, job security or similar benefit, or any enhancement to any such benefit (including acceleration of vesting or exercise of an incentive award) as a result of

the transactions contemplated under this Agreement and no agreement (whether oral or written) of the employer, with respect to a current or former employee, provides for the payment of any amounts which would fail to be deductible for federal income tax purposes by reason of Section 280G of the Code.

5.17 Disclosure. The information heretofore provided and to be provided pursuant to this Loan Agreement, including the Schedules of Exceptions and the Exhibits hereto, and each of the agreements, documents, certificates and writings previously delivered to the Lender or its representatives, do not and will not contain any untrue statement of a material fact and do not and will not omit to state a material fact required to be stated herein or therein or necessary in order to make the statements and writings contained herein and therein not false or misleading in the light of the circumstances under which they were made. To the knowledge of the Borrower, there is no fact which materially adversely affects the business, prospects or condition (financial or otherwise) of the Borrower which has not been set forth herein.

6. PAYMENT OF EXISTING DEBENTURES; CHANGE OF CONTROL.

6.1 No Optional Prepayment of Existing Debentures. Borrower may not, at any time prior to the repayment of the Loan and the satisfaction in full of the Obligations, prepay any Existing Debenture in whole or in part without the prior written consent of Lender.

6.2 Interest Payments on Existing Debentures. Notwithstanding the foregoing Section 6.1, so long as no Event of Default shall have occurred and be continuing under this Loan Agreement, the Borrower may pay to the Existing Holders regularly scheduled payments in respect of the Existing Debentures; provided, however, that the value of the aggregate amount of payments which may be made to and accepted by the Existing Holders shall not exceed Six Hundred Twenty Five Thousand Dollars (\$625,000.00) on any Interest Payment Date (as such term is defined in the Existing Debentures); and provided, further, however, that the holders of the Existing Debentures listed on Schedule I attached hereto shall have agreed that, on each Interest Payment Date while any Obligations are outstanding, such holders shall receive such payments in the capital stock and/or like debenture instruments of Borrower and not in cash or cash equivalents.

6.3 Change of Control. Upon the occurrence of a Change of Control, Borrower hereby agrees that it shall satisfy the Obligations prior to consummating any Change of Control Offer with any holder of the Existing Debentures, and shall deliver a copy of any communication with any holder of an Existing Debenture in connection with a Change of Control Offer to Lender concurrently with the delivery thereof to such holder.

7. AFFIRMATIVE COVENANTS. The Borrower hereby covenants and agrees, so long as any Obligations remain outstanding, as follows:

7.1 Maintenance of Corporate Existence, Properties and Leases; Taxes; Insurance.

(a) The Borrower shall, and shall cause the Guarantors to, maintain in full force and effect its corporate existence, rights and franchises and all material terms of licenses and other rights to use licenses, trademarks, trade names, service marks, copyrights, patents or processes owned or possessed by it and necessary to the conduct of its business.

(b) The Borrower shall, and shall cause the Guarantors to, keep each of its properties necessary to the conduct of its business in good repair, working order and condition, reasonable wear and tear excepted, and from time to time make all needful and proper repairs, renewals, replacements, additions and improvements thereto; and the Borrower shall, and shall cause the Guarantors to, at all times comply with each material provision of all leases to which it is a party or under which it occupies property.

(c) The Borrower shall, and shall cause the Guarantors to, promptly pay and discharge, or cause to be paid and discharged when due and payable, all lawful taxes, assessments and governmental charges or levies imposed upon the income, profits, assets, property or business of the Borrower and the Guarantors, and all claims or indebtedness (including, without limitation, claims or demands of workmen, materialmen, vendors, suppliers, mechanics, carriers, warehousemen and landlords) which, if unpaid might become a lien upon the assets or property of the Borrower or a Guarantor; provided, however, that any such tax, assessment, charge or levy need not be paid if the validity thereof shall be contested timely and in good faith by appropriate proceedings, if the Borrower or Guarantor shall have set aside on its books adequate reserves with respect thereto, and the failure to pay shall not be prejudicial in any material respect to the Lender; and provided, further, that the Borrower or Guarantor will pay or cause to be paid any such tax, assessment, charge or levy forthwith upon the commencement of proceedings to foreclose any lien which may have attached as security therefor. The Borrower shall, and shall cause the Guarantors to, pay or cause to be paid all other indebtedness incident to the operations of the Borrower or the Guarantors.

(d) The Borrower shall, and shall cause the Guarantors to, keep their respective assets which are of an insurable character insured by financially sound and reputable insurers against loss or damage by theft, fire, explosion and other risks customarily insured against by companies in the lines of business of the Borrower and the Guarantors, in amounts sufficient to prevent the Borrower or the Guarantors from becoming a co-insurer of the property insured; and the Borrower shall, and shall cause the Guarantors to, maintain, with financially sound and reputable insurers, insurance against other hazards and risks and liability to persons and property to the extent and in the manner customary for companies in similar businesses similarly situated or as may be required by law, including, without limitation, general liability, fire and business interruption insurance, and product liability insurance as may be required pursuant to any license agreement to which the Borrower or Guarantors are a party or by which any of them are bound.

7.2 Basic Financial Information. The Borrower shall furnish the following reports to the Lender so long as the Obligations are outstanding:

(a) within thirty (30) days after the end of each of the twelve (12) monthly accounting periods in each fiscal year (or when furnished to the Borrower's Board of Directors, if earlier), unaudited consolidated statements of income and retained earnings and cash flows of the Borrower and its Subsidiaries for each monthly period and for the period from the beginning of such fiscal year to the end of such monthly period, together with consolidated balance sheets of the Borrower and its Subsidiaries as at the end of each monthly period, setting forth in each case comparisons to budget and to corresponding periods in the preceding fiscal year, which statements will be prepared in accordance with GAAP, consistently applied;

(b) within ninety (90) days after the end of each fiscal year, consolidated statements of income and retained earnings and cash flows of the Borrower and its Subsidiaries for the period from the beginning of each fiscal year to the end of such fiscal year, and consolidated

balance sheets as at the end of such fiscal year, setting forth in each case in comparative form corresponding figures for the preceding fiscal year, which statements will be prepared in accordance with GAAP, consistently applied (except as approved by the accounting firm examining such statements and disclosed by the Borrower), and will be accompanied by:

- (i) an unqualified report of the Borrower's independent certified public accounting firm; for purposes of this Section, a report on the consolidated financial statements of the Borrower and its Subsidiaries disclosing a "going concern" paragraph shall not be considered "unqualified";
- (ii) a report from such accounting firm, addressed to the Lender, stating that in making the audit necessary to express their opinion on such financial statements, nothing has come to their attention which would lead them to believe that the Borrower is not in compliance with all the financial covenants contained in, or an event of default has occurred with respect to, any material agreements to which the Borrower or its Subsidiaries is a party or by which it is bound, including, without limitation, this Loan Agreement (an "Event of Noncompliance") or, if such accountants have reason to believe that any Event of Noncompliance has occurred, a letter specifying the nature thereof; and

(iii) the management letter of such accounting firm;

(c) within forty-five (45) days after the end of each quarterly accounting period in each fiscal year, a certificate of the Chief Financial Officer of the Borrower stating that the Borrower is in compliance with the terms of this Loan Agreement and any other material contract or commitment to which the Borrower or any of its Subsidiaries is a party or by which any of them is bound, or, if the Borrower or any of its Subsidiaries is not in compliance, specifying the nature and period of noncompliance, and what actions the Borrower or such Subsidiary has taken and/or proposes to take with respect thereto. Notwithstanding the foregoing, the certificate delivered at the end of each fiscal year of the Borrower shall be signed by both the Chief Executive Officer and the Chief Financial Officer of the Borrower and shall be delivered within ninety (90) days after the end of the fiscal year;

(d) promptly upon receipt thereof, any additional reports or other detailed information concerning significant aspects of the operations and condition, financial or otherwise, of the Borrower and its Subsidiaries, given to the Borrower by its independent accountants;

(e) at least thirty (30) days prior to the end of each fiscal year, a detailed annual operating budget and business plan for the Borrower and its Subsidiaries for the succeeding twelve-month period. Such budgets shall be prepared on a monthly basis, displaying consolidated statements of anticipated income and retained earnings, consolidated statements of anticipated cash flow and projected consolidated balance sheets, setting forth in each case the assumptions (which assumptions and projections shall represent and be based upon the good faith judgment in respect thereof of the chief executive officer of the Borrower) behind the projections contained in such financial statements, and which budgets shall have been approved by the Board of Directors of the Borrower prior to the beginning of each twelve-month period for which such budget shall have been

prepared and, promptly upon preparation thereof, any other budgets that the Borrower may prepare and any revisions of such annual or other budgets;

(f) within ten (10) days after transmission or receipt thereof, copies of all financial statements, proxy statements and reports which the Borrower sends to its stockholders or directors, and copies of all registration statements and all regular, special or periodic reports which it or any of its officers or directors files with the Commission, the American Stock Exchange (the "AMEX") or with any other securities exchange on which any of the securities of the Borrower are then listed or proposed to be listed, copies of all press releases and other statements made generally available by the Borrower to the public concerning material developments in the business of the Borrower and its Subsidiaries and copies of material communications sent to or received from stockholders, directors or committees of the Board of Directors of the Borrower or any of its Subsidiaries and copies of all material communications sent to and received from the Existing Holders or any other lender to the Borrower; and

(g) with reasonable promptness such other information and financial data concerning the Borrower as any person entitled to receive materials under this Section 7.2 may reasonably request.

7.3 Notice of Adverse Change. The Borrower shall promptly give notice to the Lender (but in any event within seven (7) days) after becoming aware of the existence of any condition or event which constitutes, or the occurrence of, any of the following:

(a) any Event of Noncompliance;

(b) any other Event of Default;

(c) the institution or threatening of institution of an action, suit or proceeding against the Borrower or any Subsidiary before any court, administrative agency or arbitrator, including, without limitation, any action of a foreign government or instrumentality, which, if adversely decided, could materially adversely affect the business, prospects, properties, financial condition or results of operations of the Borrower and its Subsidiaries, taken as a whole whether or not arising in the ordinary course of business;

(d) any information relating to the Borrower or any Subsidiary which could reasonably be expected to materially and adversely affect the assets, property, business or condition (financial or otherwise) of the Borrower or its ability to perform the terms of this Agreement; or

(e) any failure by the Borrower or its Subsidiaries to comply with the provisions of Section 7.4(b) below.

Any notice given under this Section 7.3 shall specify the nature and period of existence of the condition, event, information, development or circumstance, the anticipated effect thereof and what actions the Borrower has taken and/or proposes to take with respect thereto; or

7.4 Compliance With Agreements; Compliance With Laws. The Borrower shall comply and cause its Subsidiaries:

(a) to comply with the terms and conditions of all material agreements, commitments or instruments to which the Borrower or any of its Subsidiaries is a party or by which it or they may be bound; and

(b) to comply in all material respects with any material laws, ordinances, rules and regulations of any foreign, federal, state or local government or any agency thereof, or any writ, order or decree, and conform to all valid requirements of governmental authorities relating to the conduct of their respective businesses, properties or assets, including, but not limited to, (i) that certain Agreed Order, approved and adopted by the Indiana Department of Environmental Management on December 27, 1999, with respect to Houba's Culver, Indiana real property, and (ii) the requirements of the FDA Act, the Federal Food, Drug, and Cosmetic Act, the CSA, ERISA, Environmental Laws, the Occupational Safety and Health Act, the Foreign Corrupt Practices Act and the rules and regulations of each of the agencies administering such acts.

7.5 Protection of Licenses, etc. The Borrower shall, and shall cause its Subsidiaries to, maintain, defend and protect to the best of their ability licenses and sublicenses (and to the extent the Borrower or a Subsidiary is a licensee or sublicensee under any license or sublicense, as permitted by the license or sublicense agreement), trademarks, trade names, service marks, patents and applications therefor and other proprietary information owned or used by it or them and shall keep duplicate copies of any licenses, trademarks, service marks or patents owned or used by it, if any, at a secure place selected by the Borrower.

7.6 Accounts and Records; Inspections.

(a) The Borrower shall keep true records and books of account in which full, true and correct entries will be made of all dealings or transactions in relation to the business and affairs of the Borrower and its Subsidiaries in accordance with GAAP applied on a consistent basis.

(b) Subject to Section 12.12, the Borrower shall permit the Lender or its officers, employees or representatives during regular business hours of the Borrower, upon reasonable notice and as often as the Lender may reasonably request, to visit and inspect the offices and properties of the Borrower and its Subsidiaries and (i) to make extracts or copies of the books, accounts and records of the Borrower or its Subsidiaries, and (ii) to discuss the affairs, finances and accounts of the Borrower and its Subsidiaries, with the Borrower's (or Subsidiary's) directors and officers, its independent public accountants, consultants and attorneys.

(c) Nothing contained in this Section 7.6 shall be construed to limit any rights which the Lender may have or acquire with respect to the books and records of the Borrower and its Subsidiaries, to inspect its properties or to discuss its affairs, finances and accounts.

7.7 Independent Accountants. The Borrower will retain a firm of independent certified public accountants reasonably acceptable to the Lender (an "Approved Accounting Firm") to audit the Borrower's financial statements at the end of each fiscal year. In the event the services of the Approved Accounting Firm or any firm of independent public accountants hereafter employed by the Borrower are terminated, the Borrower will promptly thereafter request the firm of independent public accountants whose services are terminated to deliver to the Lender a letter of such firm setting forth its understanding as to the reasons for the termination of their services and whether there were, during the two most recent fiscal years or such shorter period during which said firm had been retained by the Borrower any disagreements between them and the Borrower on any matter of

accounting principles or practices, financial statement disclosure, or auditing scope or procedure. In its notice, the Borrower shall state whether the change of accountants was recommended or approved by the Board of Directors or any committee thereof. In the event of such termination, the Borrower will promptly thereafter engage another Approved Accounting Firm.

7.8 Board Meetings; Observer Rights.. The Borrower agrees to hold meetings of its Board of Directors at least four (4) times a year, at no more than three-month intervals. The Lender shall have the right, at all times so long as the Obligations are outstanding, to designate one person to attend all meetings of the Board of Directors or committees thereof as an observer; and Borrower shall deliver to Lender all written materials provided to the members of its Board of Directors or committees thereof, concurrently with the delivery of such materials to such members, provided, however, that the Borrower may exclude Lender from any bona fide discussions, and shall not be obligated to provide materials (i) regarding the relationship between Lender and Borrower under this Loan Agreement and the various agreements between Borrower and Lender contemplated hereby and (ii) which are communications between Borrower and its attorneys of a type which would be considered subject to attorney-client privilege.

7.9 Maintenance of Office. The Borrower will maintain its principal office at the address of the Borrower set forth in Section 12.7 of this Loan Agreement where notices, presentments and demands in respect of any of the Loan Documents may be made upon the Borrower, until such time as the Borrower shall notify the Lender in writing, at least thirty (30) days prior thereto, of any change of location of such office.

7.10 Use of Proceeds. The Borrower shall use all the Loan proceeds only as provided in Section 7.10 to the Schedule of Exceptions.

7.11 Payment of Note; Prepayment. The Borrower shall pay the principal of and interest on the Loan in the time, the manner and the form provided in the Note. The Borrower may, upon at least three Business Days' prior written notice to Lender, prepay the Note, in whole or in part, along with accrued, unpaid interest to the date of such prepayment on the amount repaid.

7.12 Reporting Requirements. The Borrower shall comply with its reporting and filing obligations pursuant to Section 13 or 15(d) of the Exchange Act. The Borrower shall provide copies of such reports, including, without limitation, reports on Form 10-K, 10-Q, 8-K and Schedule 14A promulgated under the Exchange Act, or substantially the same information required to be contained in any successor form, to the Lender promptly upon filing with the Commission.

7.13 Further Assurances. From time to time the Borrower shall execute and deliver to the Lender and the Lender shall execute and deliver to the Borrower such other instruments, certificates, agreements and documents and take such other action and do all other things as may be reasonably requested by the other party in order to implement or effectuate the terms and provisions of this Loan Agreement and any of the Loan Documents.

7.14 Default Notices. Borrower shall deliver to Lender copies of any Default Notice it receives in connection with the Existing Debentures.

7.15 Immaterial Subsidiaries. So long as any Obligations are outstanding, Borrower shall not permit any of the Immaterial Subsidiaries to commence any business operations of a type or

scope not currently conducted by them, nor permit any Immaterial Subsidiary to acquire any rights or property not currently owned by it.

8. **NEGATIVE COVENANTS.** The Borrower hereby covenants and agrees, so long as any Obligations are outstanding, it will not (and not allow any of its Subsidiaries to), directly or indirectly, without the prior written consent of the Lender, as follows:

8.1 **Payment of Dividends; Stock Purchase.** Declare or pay any cash dividends on, or make any distribution to the holders of, any shares of capital stock of the Borrower, other than dividends or distributions payable in such capital stock, or purchase, redeem or otherwise acquire or retire for value any shares of capital stock of the Borrower or warrants or rights to acquire such capital stock.

8.2 **Stay, Extension and Usury Laws.** At any time insist upon, plead, or in any manner whatsoever claim or take the benefit or advantage of, any stay, extension or usury law wherever enacted, now or at any time hereinafter in force, which may affect the covenants or the performance of the Loan Documents, the Borrower hereby expressly waiving all benefit or advantage of any such law, or by resort to any such law, hinder, delay or impede the execution of any power herein granted to the Lender but will suffer and permit the execution of every such power as though no such law had been enacted.

8.3 **Liens.** Except as otherwise provided in this Loan Agreement, create, incur, assume or permit to exist any mortgage, pledge, lien, security interest or encumbrance on any part of its properties or assets, or on any interest it may have therein, now owned or hereafter acquired, nor acquire or agree to acquire property or assets under any conditional sale agreement or title retention contract, except that the foregoing restrictions shall not apply to:

(a) liens for taxes, assessments and other governmental charges, if payment thereof shall not at the time be required to be made, and provided such reserve as shall be required by GAAP consistently applied shall have been made therefor;

(b) liens of workmen, materialmen, vendors, suppliers, mechanics, carriers, warehouseman and landlords or other like liens, incurred in the ordinary course of business for sums not then due or being contested in good faith, if an adverse decision in which contest would not materially affect the business of the Borrower;

(c) liens securing indebtedness of the Borrower or any Subsidiaries which is in an aggregate principal amount not exceeding \$500,000, and which liens are subordinate to liens on the same assets held by the Lender;

(d) statutory liens of landlords, statutory liens of banks and rights of set-off, and other liens imposed by law, in each case incurred in the ordinary course of business (i) for amounts not yet overdue or (ii) for amounts that are overdue and that are being contested in good faith by appropriate proceedings, so long as such reserves or other appropriate provisions, if any, as shall be required by GAAP shall have been made for any such contested amounts;

(e) liens incurred or deposits made in the ordinary course of business in connection with workers' compensation, unemployment insurance and other types of social security, or to secure the performance of tenders, statutory obligations, surety and appeal bonds, bids, leases,

government contracts, trade contracts, performance and return-of-money bonds and other similar obligations (exclusive of obligations for the payment of borrowed money);

(f) any attachment or judgment lien not constituting an Event of Default;

(g) easements, rights-of-way, restrictions, encroachments, and other minor defects or irregularities in title, in each case which do not and will not interfere in any material respect with the ordinary conduct of the business of the Borrower or any of its Subsidiaries;

(h) any (i) interest or title of a lessor or sublessor under any lease, (ii) restriction or encumbrance that the interest or title of such lessor or sublessor may be subject to, or (iii) subordination of the interest of the lessee or sublessee under such lease to any restriction or encumbrance referred to in the preceding clause (ii), so long as the holder of such restriction or encumbrance agrees to recognize the rights of such lessee or sublessee under such lease;

(i) liens in favor of customs and revenue authorities arising as a matter of law to secure payment of customs duties in connection with the importation of goods;

(j) any zoning or similar law or right reserved to or vested in any governmental office or agency to control or regulate the use of any real property;

(k) liens securing obligations (other than obligations representing debt for borrowed money) under operating, reciprocal easement or similar agreements entered into in the ordinary course of business of the Borrower and its Subsidiaries;

(l) the liens securing the Borrower's and the Guarantor's obligations under the Existing Debentures, which liens are subordinate to liens on the same assets held by the Lender;

(m) the liens listed in Section 8.3 of the Schedule of Exceptions ("Permitted Liens"); and

(n) the replacement, extension or renewal of any lien permitted by this Section 8.3 upon or in the same property theretofore subject or the replacement, extension or renewal (without increase in the amount or change in any direct or contingent obligor) of the indebtedness secured thereby.

8.4 Indebtedness. Create, incur, assume, suffer, permit to exist, or guarantee, directly or indirectly, any indebtedness, excluding, however, from the operation of the covenant:

(a) any indebtedness or the incurring, creating or assumption of any indebtedness secured by liens permitted by the provisions of Section 8.3(c) above;

(b) the endorsement of instruments for the purpose of deposit or collection in the ordinary course of business;

(c) indebtedness which may, from time to time be incurred or guaranteed by the Borrower which in the aggregate principal amount does not exceed \$500,000 and is subordinate to the indebtedness under this Agreement;

(d) indebtedness existing on the date hereof and described in Section 8.4 of the Schedule of Exceptions;

(e) indebtedness relating to contingent obligations of the Borrower and its Subsidiaries under guaranties in the ordinary course of business of the obligations of suppliers, customers, and licensees of the Borrower and its Subsidiaries;

(f) indebtedness relating to loans from the Borrower to its Subsidiaries;

(g) indebtedness relating to capital leases in an amount not to exceed \$500,000;

(h) indebtedness under the Existing Debentures;

(i) accounts or notes payable arising out of the purchase of merchandise or services in the ordinary course of business; or

(j) indebtedness (if any) expressly permitted by, and in accordance with, the terms and conditions of this Loan Agreement.

For purposes hereof, the term "indebtedness" shall mean and include (A) all items which would be included on the liability side of a balance sheet of the Borrower (or a Subsidiary) as of the date on which indebtedness is to be determined, excluding capital stock, surplus, capital and earned surplus reserves, which, in effect, were appropriations of surplus or offsets to asset values (other than reserves in respect of obligations, the amount, applicability or validity of which is, at such date, being contested by such corporation), deferred credits of amounts representing capitalization of leases; (B) the full amount of all indebtedness of others guaranteed or endorsed (otherwise than for the purpose of collection) by the Borrower (or Subsidiary) for which the Borrower (or Subsidiary) is obligated, contingently or otherwise, to purchase or otherwise acquire, or for the payment or purchase of which the Borrower (or Subsidiary) has agreed, contingently or otherwise, to advance or supply funds, or with respect to which the Borrower (or Subsidiary) is contingently liable, including, without limitation, indebtedness for borrowed money and indebtedness guaranteed or supported indirectly by the Borrower (or Subsidiary) through an agreement, contingent or otherwise (1) to purchase the indebtedness, or (2) to purchase, sell, transport or lease (as lessee or lessor) property, or to purchase or sell services at prices or in amounts designed to enable the debtor to make payment of the indebtedness or to assure the owner of the indebtedness against loss, or (3) to supply funds to or in any other manner invest in the debtor; and (C) indebtedness secured by any mortgage, pledge, security interest or lien whether or not the indebtedness secured thereby shall have been assumed; provided, however, that such term shall not mean and include any indebtedness (x) in respect to which monies sufficient to pay and discharge the same in full shall have been deposited with a depository, agency or trustee in trust for the payment thereof, or (y) as to which the Borrower (or Subsidiary) is in good faith contesting, provided that an adequate reserve therefor has been set up on the books of the Borrower (or Subsidiary).

8.5 Merger, Consolidation, etc. Merge or consolidate with any person (except that the Borrower may merge with any wholly-owned Subsidiary so long as the Borrower is the surviving corporation in such merger), or sell, transfer, lease or otherwise dispose of 10% or more of its consolidated assets (as shown on the most recent financial statements of the Borrower or the Subsidiary, as the case may be) in any single transaction or series of related transactions (other than the sale of inventory in the ordinary course of business), or liquidate, dissolve, recapitalize or

reorganize in any form of transaction, or acquire all or substantially all of the capital stock or assets of another business or entity.

8.6 Amendment of Charter Documents. Make any amendment to the Certificate of Incorporation as heretofore amended, or By-Laws, as heretofore amended, of the Borrower or the Certificate of Incorporation or By-Laws of either Guarantor, which amendment would interfere in any material respect with the payment by Borrower, or guaranty by the Guarantors, of the Obligations or the performance by Borrower or the Guarantors of their respective obligations under the Loan Documents or the Product Agreements.

8.7 Loans and Advances. Except for loans and advances outstanding as of the Closing Date and set forth in Section 8.7 of the Schedule of Exceptions, directly or indirectly, make any advance or loan to, or guarantee any obligation of, any person, firm or entity, except for (i) loans to employees of the Borrower not in excess of \$25,000 to any one employee or \$100,000 in the aggregate where such loan(s) are necessary under exigent circumstances of such employee(s) as determined by the Board of Directors, or (ii) intercompany loans or advances and those provided for in this Loan Agreement.

8.8 Intercompany Transfers; Transactions With Affiliates; Diversion of Corporate Opportunities.

(a) Make any intercompany transfers of monies or other assets in any single transaction or series of transactions, except as otherwise permitted in this Loan Agreement.

(b) Engage in any transaction with any of the officers, directors, employees or affiliates of the Borrower or of its Subsidiaries, except on terms no less favorable to the Borrower or the Subsidiary as could be obtained at Arm's Length (as hereinafter defined).

(c) Divert (or permit anyone to divert) any business or opportunity of the Borrower or Subsidiary to any other corporate or business entity.

8.9 Personal Expenses. Except as set forth in Section 8.9 of the Schedule of Exceptions, permit any person to charge to the Borrower (or any of its Subsidiaries) any expense not directly related to the business of the Borrower (or Subsidiary), including, without limitation, expenses for country and health club membership fees and expenses, and personal travel and entertainment expenses, or reimburse such person for any such expense.

8.10 Other Business. Enter into or engage, directly or indirectly, in any business other than the business currently conducted or proposed to be conducted by the Borrower or any Subsidiary.

8.11 Investments. Make any investments in, or purchase any stock, option, warrant, or other security or evidence of indebtedness of, any person or entity (exclusive of any Subsidiary), other than obligations of the United States Government or certificates of deposit or other instruments maturing within one year from the date of purchase from financial institutions with capital in excess of \$100 million.

8.12 Employee Benefit Plans and Compensation. Except as contemplated by this Loan Agreement:

(a) enter into any agreement to provide for or otherwise establish any written or unwritten employee benefit plan, program or other arrangement of any kind, covering current or former employees of the Borrower or its Subsidiaries except for (i) any such plan, program or arrangement expressly permitted under an agreement listed in Section 8.12 of the Schedule of Exceptions, and (ii) any such plan, program or arrangement which a company similar to the Borrower in size and financial condition, and which is engaged in a business substantially similar to the business of the Borrower and its Subsidiaries, would establish or implement for the benefit of its employees in the ordinary course of business; provided, however, that no such plan, program or arrangement may be established or implemented if such action would have a material affect on the terms of employment of the employees of the Borrower or its Subsidiaries, or

(b) provide for or agree to any material increase in any benefit provided to current or former employees of the Borrower or its Subsidiaries over that which is provided to such individuals pursuant to a plan or arrangement disclosed in Section 5.16 of the Schedule of Exceptions as of the Closing Date. For purpose of this Section, a "material increase" shall not include any cost of living increase or similar regular increase agreed to pursuant to the Collective Bargaining Agreement between the Borrower and the Drug, Chemical, Cosmetic, Plastics and Affiliated Industries Warehouse Employees Local 815, International Brotherhood of Teamsters.

(c) provide for or agree to any increase in the annual compensation of any of the employees of the Borrower or its Subsidiaries, except for (i) annual salary increases not to exceed a ten percent (10%) increase over such employee's annual salary compensation on the date hereof, and (ii) normal and customary annual bonuses to employees not to exceed an aggregate Three Hundred Fifty Thousand Dollars (\$350,000) in any fiscal year.

8.13 Capital Expenditures. Other than for a capital expenditure contained in any budget approved by the Board of Directors, or capital expenditures not contained in any such budget, but which do not exceed \$250,000 in the aggregate during any fiscal year of the Borrower, make or commit to make any capital expenditures.

8.14 Arm's Length Transactions. Enter into any transaction, contract or commitment or take any action other than at Arm's Length. For purposes hereof the term "Arm's Length" means a transaction or negotiation in which each party is completely independent of the other, seeks to obtain terms which are most favorable to it and has no economic or other interest in making concessions to the other party.

9. EVENTS OF DEFAULT

9.1 Events of Default. The occurrence of any of the following events (an "Event of Default") shall be deemed an event of default hereunder.

(a) if the Borrower shall default in the payment of (i) any part of the principal of the Loan, when the same shall become due and payable, whether at maturity or at a date fixed for prepayment or by acceleration or otherwise; or (ii) the interest on the Loan; when the same shall become due and payable or within two (2) Business Days thereafter;

(b) if the Borrower shall default in the performance of any of the covenants contained herein and such default shall have continued without cure for fifteen (15) days after written

notice thereof (a "Default Notice") is given to the Borrower with respect to such covenant by the Lender;

(c) if the Borrower shall default in the performance of any other material agreement or covenant contained in the Loan Documents and such default shall not have been remedied to the satisfaction of the Lender within thirty-five (35) days after a Default Notice shall have been given to the Borrower;

(d) if any representation or warranty made in this Loan Agreement or in or any certificate delivered pursuant hereto shall prove to have been incorrect in any material respect when made;

(e) if any default shall occur under any indenture, mortgage, agreement, instrument or commitment evidencing or under which there is at the time outstanding any indebtedness of the Borrower or a Subsidiary, in excess of \$100,000, or which results in such indebtedness, in an aggregate amount (with other defaulted indebtedness) in excess of \$250,000 becoming due and payable prior to its due date and if such indenture or instrument so requires, the holder or holders thereof (or a trustee on their behalf) shall have declared such indebtedness due and payable;

(f) if any of the Borrower or its Subsidiaries shall default in the observance or performance of any material term or provision of:

(i) any of the Product Agreements; or

(ii) an agreement to which it is a party or by which it is bound which default will have a material adverse effect on the Borrower and its Subsidiaries, taken as a whole;

and such default is not waived or cured within the applicable grace period;

(g) if a final judgment which, either alone or together with other outstanding final judgments against the Borrower and its Subsidiaries, exceeds an aggregate of \$250,000 shall be rendered against the Borrower or any Subsidiary and such judgment shall have continued undischarged or unstayed for thirty-five (35) days after entry thereof;

(h) if the Borrower or any Subsidiary shall make an assignment for the benefit of creditors, or shall admit in writing its inability to pay its debts; or if the Borrower or any Subsidiary shall suffer a receiver or trustee for it or substantially all of its assets to be appointed, and, if appointed without its consent, not to be discharged or stayed within ninety (90) days; or if the Borrower or any Subsidiary shall suffer proceedings under any law relating to bankruptcy, insolvency or the reorganization or relief of debtors to be instituted by or against it, and, if contested by it, not to be dismissed or stayed within ninety (90) days; or if the Borrower or any Subsidiary shall suffer any writ of attachment or execution or any similar process to be issued or levied against it or any significant part of its property which is not released, stayed, bonded or vacated within ninety (90) days after its issue or levy; or if the Borrower or any Subsidiary takes corporate action in furtherance of any of the aforesaid purposes or conditions; or

(i) if any Event of Default shall occur and be continuing under the terms of the Existing Debentures, and the Majority Holders (as defined in the Existing Debentures) shall have declared such indebtedness due and payable.

9.2 Remedies.

(a) Upon the occurrence of an Event of Default, Lender may, at any time, unless all defaults shall theretofore have been remedied, at its option, by written notice or notices to Borrower (i) declare the Loan to be due and payable, whereupon the same shall forthwith mature and become due and payable, together with interest accrued thereon, without presentment, demand, protest or notice, all of which are hereby waived; and (ii) declare any other amounts payable to Lender under the Loan Documents or as contemplated hereby due and payable.

(b) Upon the occurrence of any of the Events of Default described in Section 9.1(h) above, then, automatically and whether or not notice is given, (i) the Loan shall become immediately due and payable, together with interest accrued thereon, without presentment, demand, protest or notice, all of which are hereby waived; and (ii) any other amounts payable to Lender under the Loan Documents or as contemplated hereby shall become immediately due and payable.

(c) Notwithstanding anything contained in Section 9.2(a), in the event that at any time after the principal of the Loan shall so become due and payable and prior to the date of maturity stated in the Note, and all arrears of principal of and interest on the Loan (with interest at the rate specified in the Note on any overdue principal and, to the extent legally enforceable, on any interest overdue) shall be paid by or for the account of Borrower, then Lender, by written notice or notices to Borrower, may (but shall not be obligated to) waive such Event of Default and its consequences and rescind or annul such declaration, but no such waiver shall extend to or affect any subsequent Event of Default or impair any right resulting therefrom.

9.3 Enforcement. In case any one or more Events of Default shall occur and be continuing, Lender may proceed to protect and enforce its rights by an action at law, suit in equity or other appropriate proceeding, whether for the specific performance of any agreement contained herein or in the Note or for an injunction against a violation of any of the terms hereof or thereof, or in aid of the exercise of any power granted hereby or thereby or by law. In case of a default in the payment of any principal of or interest on the Loan, Borrower will pay to Lender such further amount as shall be sufficient to cover the cost and the expenses of collection, including, without limitation, reasonable attorneys' fees, expenses and disbursements. No course of dealing and no delay on the part of Lender in exercising any rights shall operate as a waiver thereof or otherwise prejudice Lender's rights. No right conferred hereby or by the Note upon Lender shall be exclusive of any other right referred to herein or therein or now available at law in equity, by statute or otherwise.

10. AMENDMENT AND WAIVER. This Agreement may not be amended, discharged or terminated (or any provision hereof waived) without the written consent of the Borrower and Lender.

11. INDEMNITY, ETC. The Borrower shall:

(a) pay, and hold the Lender harmless from and against, any and all present and future stamp, excise and other similar taxes with respect to the foregoing matters and hold the Lender

harmless from and against any and all liabilities with respect to or resulting from any delay or omission (other than to the extent attributable to the Lender) to pay such taxes; and

(b) indemnify the Lender, each of its Affiliates and their respective officers, directors, employees, representatives, attorneys and agents (each an "Indemnatee") from, and hold each of them harmless against, any and all losses, liabilities, claims, damages, expenses, obligations, penalties, actions, judgments, suits, costs or disbursements of any kind or nature whatsoever (including, without limitation, the reasonable fees and disbursements of counsel for such Indemnatee) that may at any time (including, without limitation, at any time following the payment of the Obligations) be imposed on, asserted against or incurred by any Indemnatee as a result of, or arising out of, or in any way related to or by reason of, or in connection with the preparation for a defense of, any investigation, litigation or proceeding arising out of, related to or in connection with (i) the execution, delivery or performance of any Loan Document (including, without limitation, any actual or proposed use by the Borrower or its Subsidiaries of the proceeds of the Loan), (ii) any violation by the Borrower or its Subsidiaries of any applicable Environmental Law, (iii) any Environmental Claim arising out of the management, use, control, ownership or operation of property or assets by the Borrower or its Subsidiaries, including, without limitation, all on-site and off-site activities involving Materials of Environmental Concern, (iv) the breach of any environmental representation or warranty set forth in Section 5.14, (v) the grant to the Lender of any Lien in any property or assets of the Borrower or its Subsidiaries or any stock or other equity interest in the Guarantors, and (vi) the exercise by the Lender of its rights and remedies (including, without limitation, foreclosure) under any agreements creating any such Lien (but excluding, as to any Indemnatee, any such losses, liabilities, claims, damages, expenses, obligations, penalties, actions, judgments, suits, costs or disbursements incurred solely by reason of the gross negligence or willful misconduct of such Indemnatee as finally determined by a court of competent jurisdiction). The Borrower's obligations under this Section shall survive the termination of this Loan Agreement and the payment of the Obligations.

12. MISCELLANEOUS

12.1 Definitions.

"1998 Debenture Agreement" is defined in the Recitals.

"1999 Debenture Agreement" is defined in the Recitals.

"412 Plan" is defined in Section 5.16(d).

"Affiliate" shall mean any entity which controls, is controlled by or is under common control with another entity. An entity is deemed to be in control of another entity (controlled entity) if the former owns directly or indirectly at least the lesser of (a) fifty percent (50%), or (b) the maximum percentage allowed by law in the country of the controlled entity, of the outstanding voting equity of the controlled entity.

"Agent" shall mean Galen Partners III, L.P., in its capacity as agent for the holders of the Galen Debentures.

"AMEX" is defined in Section 7.2(f).

"Approved Accounting Firm" is defined in Section 7.7.

"Arm's Length" is defined in Section 8.14.

"Borrower" is defined in the Introduction.

"Brooklyn Facility Lease" shall mean that certain real property lease, dated October 1994, by and between the Borrower and Atlantic Properties Company.

"Business Day" shall mean any day other than a Saturday, Sunday or day which banks are generally closed in the State of California.

"Change of Control" shall mean the occurrence of any of the following: (i) the consummation of any transaction the result of which is that any Person or group (as such term is used in Section 13(d)(3) of the Exchange Act), other than Galen, Oracle or any affiliate thereof or any group comprised of any of the foregoing, owns, directly or indirectly, thirty percent (30%) of the Common Equity of the Borrower, (ii) the Borrower consolidates with, or merges with or into, another Person (other than a direct or indirect wholly-owned Subsidiary) or sells, assigns, conveys, transfers, leases or otherwise disposes of all or substantially all of the Borrower's assets or the assets of the Borrower and its Subsidiaries taken as a whole to any person, or any person consolidates with, or merges with or into, the Borrower, in any such event pursuant to a transaction in which the outstanding Voting Stock of the Borrower, as the case may be, is converted into or changed for cash, securities or other property, other than any such transaction where the outstanding Voting Stock of the Borrower, as the case may be, is converted into or exchanged for Voting Stock of the surviving or transferee corporation and the beneficial owners of the Voting Stock of the Borrower immediately prior to such transaction own, directly or indirectly, not less than a majority of the Voting Stock of the surviving or transferee corporation immediately after such transaction, (iii) the Borrower, either individually or in conjunction with one or more Subsidiaries sells, assigns, conveys, transfers, leases or otherwise disposes of, or the Subsidiaries sell, assign, convey, transfer, lease or otherwise dispose of, all or substantially all of the properties and assets of the Borrower and its Subsidiaries, taken as a whole (either in one transaction or a series of related transactions), including capital stock of the Subsidiaries, to any person (other than the Borrower or a wholly owned Subsidiary of the Borrower), or (iv) during any two (2) year period commencing subsequent to the date of this Loan Agreement, individuals who at the beginning of such period constituted the Board of Directors of the Borrower (together with any new directors whose election by such Board of Directors or whose nomination for election by the stockholders of the Borrower was approved by a vote of two-thirds of the directors then still in office) who were either directors at the beginning of such period or whose election or nomination for election was previously so approved cease for any reason to constitute a majority of the Board of Directors then in office; provided, however, that a Person shall not be deemed to have ceased being a director for such purpose if such Person shall have resigned or died or if the involuntary removal of such Person was made at the direction of Persons holding a majority in principal amount of the outstanding Existing Debentures.

"Change of Control Offer" shall mean the offer required to be made to the Existing Holders in accordance with the terms of the Existing Debentures in connection with a Change in Control transaction.

"Closing" is defined in Section 3.

"Closing Date" is defined in Section 3.

"Code" shall mean the Internal Revenue Code of 1986, as amended.

"Commission" shall mean the United States Securities and Exchange Commission, and any successor agency.

"Common Equity" means all capital stock of the Borrower that is generally entitled to vote on the election of directors.

"Confidential Information" shall mean, with respect to a party, all information of any kind whatsoever (including without limitation, data, compilations, formulae, models, patent disclosures, procedures, processes, projections, protocols, results of experimentation and testing, specifications, strategies and techniques), and all tangible and intangible embodiments thereof of any kind whatsoever (including without limitation, apparatus, compositions, documents, drawings, machinery, patent applications, records and reports), which is disclosed by such party to the other party and is marked, identified as or otherwise acknowledged to be confidential at the time of disclosure to the other party. Notwithstanding the foregoing, Confidential Information of a party shall not include information which the other party can establish by written documentation (a) to have been publicly known prior to disclosure of such information by the disclosing party to the other party, (b) to have become publicly known, without fault on the part of the other party, subsequent to disclosure of such information by the disclosing party to the other party, (c) to have been received by the other party at any time from a source, other than the disclosing party, rightfully having possession of and the right to disclose such information, (d) to have been otherwise known by the other party prior to disclosure of such information by the disclosing party to the other party, or (e) to have been independently developed by employees or agents of the other party without use of such information disclosed by the disclosing party to the other party.

"Congers Facility Lease" shall mean that certain real property lease, dated March 17, 1999, by and between the Borrower and Par Pharmaceutical, Inc.

"CSA" is defined in Section 5.9(c).

"DEA" is defined in Section 5.9(c).

"Default Notice" is defined in Section 9.1(b).

"Environmental Claim" shall mean, with respect to any Person, any notice, claim, demand or similar communication (written or oral) by any other Person alleging potential liability for investigatory costs, cleanup costs, governmental response costs, natural resources damages, property damages, personal injuries, fines or penalties arising out of, based on or resulting from (i) the presence, or release into the environment, of any Material of Environmental Concern at any location, whether or not owned by such Person or (ii) circumstances forming the basis of any violation, or alleged violation, of any Environmental Law.

"Environmental Law" shall mean all federal, state, local and foreign laws and regulations relating to pollution or protection of human health, safety or the environment (including, without limitation, ambient air, surface water, ground water, land surface or subsurface strata), including without limitation, laws and regulations relating to emissions, discharges, releases or threatened

releases of Materials of Environmental Concern, or otherwise relating to the manufacture, processing, distribution, use, treatment, storage, disposal, transport or handling of Materials of Environmental Concern.

"ERISA" is defined in Section 5.16(a).

"ERISA Affiliate" is defined in Section 5.16(a).

"Event of Default" is defined in Section 9.1.

"Event of Noncompliance" is defined in Section 7.2(ii).

"Exchange Act" shall mean the Securities Exchange Act of 1934, as amended.

"Existing Debentures" is defined in the Recitals.

"Existing Holders" is defined in the Recitals.

"FDA" is defined in Section 5.9(b).

"FDC Act" is defined in Section 5.9(b).

"Federal Food, Drug, and Cosmetic Act" shall mean the Federal Food, Drug, and Cosmetic Act, 21 USC Sections 301 et seq.

"Financing Statements" is defined in Section 4.7(a).

"GAAP" is defined in Section 5.8(b).

"Galen Debentures" is defined in the Recitals.

"Guarantors" shall mean Halsey Pharmaceutical, Inc., a Delaware corporation, and Houba, Inc., an Indiana corporation, both wholly-owned Subsidiaries of the Borrower.

"Houba" shall mean Houba, Inc., an Indiana corporation and a wholly-owned Subsidiary of the Borrower.

"Immaterial Subsidiaries" is defined in Section 5.2.

"Indemnatee" is defined in Section 11(b).

"Intellectual Property Rights" is defined in Section 5.11(a).

"IRS" shall mean the United States Internal Revenue Service, and any successor corporation.

"Lender" is defined in the Introduction.

"Loan" is defined in Section 1.1.

"Loan Agreement" is defined in the Introduction.

"Loan Documents" is defined in Section 2.3.

"Materials of Environmental Concern" shall mean and include chemicals, pollutants, contaminants, wastes, toxic substances, petroleum and petroleum products, asbestos and radioactive materials.

"Negotiation Agreement" is defined in the Recitals.

"Note" is defined in Section 1.2.

"Obligations" shall mean all obligations, liabilities and indebtedness of every kind, nature and description of the Borrower and the Guarantors from time to time owing to the Lender or any Indemnatee under or in connection with the Loan Documents, whether direct or indirect, primary or secondary, joint or several, absolute or contingent, due or to become due, now existing or hereafter arising and however acquired and shall include, without limitation, all principal and interest on the Loan and, to the extent chargeable under any Loan Document, all charges, expenses, fees and reasonable attorney's fees.

"Oracle Debentures" is defined in the Recitals.

"PCB" is defined in Section 5.14(c).

"Permitted Liens" is defined in Section 8.3.

"Person" shall mean any individual, partnership, limited liability company, joint venture, firm, corporation, association, trust or other enterprise or any government or political subdivision or any agency, department or instrumentality thereof.

"Plan" and "Plans" are defined in Section 5.16(a).

"Product" is defined in the Recitals.

"Product Agreements" shall mean the Purchase Agreement, the Supply Agreements and the Negotiation Agreement, and any supply agreements entered into after the date hereof pursuant to the terms as contemplated in the Negotiation Agreement, collectively. "Product Agreement" shall mean any of the Product Agreements.

"Purchase Agreement" is defined in the Recitals.

"Reportable Event" is defined in Section 5.16(m).

"Schedule of Exceptions" is defined in Section 5.1.

"Selected Reports" is defined in Section 5.1.

"Subsidiary" is defined in Section 5.2.

"Subordination Agreement" is defined in the Recitals.

"Supply Agreements" is defined in the Recitals.

"Tax Qualified Plan" is defined in Section 5.16(s).

"Unfunded Pension Liability" is defined in Section 5.16(e).

"Voting Agreement" mean securities of any class of capital stock of the Borrower entitling the holders thereof to vote in the election of members of the Board of Directors of the Borrower.

"Watson Collateral Assignments" is defined in Section 2.1.

"Watson Guaranty" is defined in Section 2.2.

"Watson Guarantors Collateral Assignment" is defined in Section 2.3.

"Watson Guarantors Security Agreement" is defined in Section 2.3.

"Watson Mortgage" is defined in Section 2.3.

"Watson Security Agreement" is defined in Section 2.1.

"Watson Security Documents" is defined in Section 2.3.

"Watson Stock Pledge Agreement" is defined in Section 2.1.

"Withdrawal Liability" is defined in Section 5.16(g).

12.2 Right of Setoff. In addition to any rights now or hereafter granted under applicable law or otherwise, and not by way of limitation of any such rights, upon the occurrence and during the continuance of any Event of Default, the Lender is hereby authorized at any time or from time to time, without presentment, demand, protest or other notice of any kind to the Borrower or any Guarantor or to any other Person, any such notice being hereby expressly waived, to set off and to appropriate and apply any and all indebtedness at any time held or owing by the Lender to or for the credit or the account of the Borrower or its Subsidiaries, or any payment due Borrower from Lender under the Product Agreements, against and on account of the Obligations or under any of the other Loan Documents and all other claims of any nature or description arising out of or connected with this Loan Agreement or any other Loan Document, irrespective of whether or not such Lender shall have made any demand hereunder and although said Obligations, liabilities or claims, or any of them, shall be contingent or unmatured.

12.3 Governing Law. This Agreement and the rights of the parties hereunder shall be governed in all respects by the laws of the State of California wherein the terms of this Loan Agreement were negotiated.

12.4 Survival. Except as specifically provided herein, the representations, warranties, covenants and agreements made herein shall survive (a) any investigation made by Lender, and (b) the Closing.

12.5 Successors and Assigns. Except as otherwise expressly provided herein, the provisions hereof shall inure to the benefit of, and be binding upon and enforceable by and against, the successors, assigns, heirs, executors and administrators of the parties hereto.

12.6 Entire Agreement. This Agreement and the Product Agreements (including the exhibits hereto and thereto) and the other documents delivered pursuant hereto and simultaneously herewith constitute the full and entire understanding and agreement between the parties with regard to the subject matter hereof and thereof.

12.7 Notices. All notices, demands or other communications given hereunder shall be in writing and shall be sufficiently given if delivered either personally, by fax (receipt confirmed by recipient or followed by copy sent via the other means set forth herein) or by a nationally recognized courier service marked for next Business Day delivery or sent in a sealed envelope by first class mail, postage prepaid and either registered or certified, addressed as follows.

If to Borrower:

Halsey Drug Co., Inc.
695 No. Perryville Road
Rockford, Illinois 61107
Fax no. (815) 399-9710
Attn: Mr. Michael Reicher
Chief Executive Officer

If to Lender:

Chief Financial Officer
Watson Pharmaceuticals, Inc.
311 Bonnie Circle
Corona, California 92880
Fax no. (909) 279-8094
cc: Mr. Robert Funsten
General Counsel

or to such other address with respect to any party hereto as such party may from time to time notify (as provided above) the other party hereto. Any such notice, demand or communication shall be deemed to have been given (i) on the date of delivery, if delivered personally, (ii) on the date of facsimile transmission, receipt confirmed, (iii) one Business Day after delivery to a nationally recognized overnight courier service, if marked for next day delivery or (iv) five Business Days after the date of mailing, if mailed. Copies of any notice, demand or communication given to (x) Borrower shall be delivered to St. John & Wayne, L.L.C., Two Penn Plaza East, Newark, New Jersey, 07105-2249, fax no. (973) 491-3555, Attn.: John P. Reilly, or such other address as may be directed and (y) Lender shall be delivered to Stradling Yocca Carlson & Rauth, A Professional Corporation, 660 Newport Center Drive, Newport Beach, California, 92660, fax no. (949) 725-4100, Attn: Lawrence B. Cohn, or such other address as may be directed.

12.8 Delays or Omissions. No delay or omission to exercise any right, power or remedy accruing to Lender upon any breach or default of Borrower under this Loan Agreement shall impair any such right, power or remedy of Lender nor shall it be construed to be a waiver of any such breach or default, or an acquiescence, therein, or of or in any similar breach or default thereafter occurring; nor shall any waiver of any single breach or default be deemed a waiver of any other breach or default theretofore or thereafter occurring. Any waiver, permit, consent or approval of any kind or character on the part of Lender of any breach or default under this Loan Agreement, or any waiver on the part of Lender of any provisions or conditions of this Loan Agreement must be made in writing and shall be effective only to the extent specifically set forth in such writing. All remedies, either under this Loan Agreement or by law or otherwise afforded to Lender shall be cumulative and not alternative.

12.9 Rights; Severability. Unless otherwise expressly provided herein, Lender's rights hereunder are several rights, not rights jointly held with any other person. In case any provision of

this Loan Agreement shall be invalid, illegal or unenforceable, the validity, legality and enforceability of the remaining provisions shall not in any way be affected or impaired thereby.

12.10 Expenses. Borrower shall bear its own expenses and legal fees incurred on its behalf with respect to the negotiation, execution and consummation of the Loan Documents and the Product Agreements, and Borrower will reimburse Lender for all of the reasonable expenses incurred by Lender with respect to the negotiation, execution and consummation of the transactions contemplated by the Loan Documents and the Product Agreements, and due diligence conducted in connection therewith, including the reasonable fees and disbursements of Lender's counsel; provided, however, that the amount of such reimbursement shall not exceed \$50,000. Such reimbursement shall be paid on the Closing Date.

12.11 Litigation. The parties each hereby waive trial by jury in any action or proceeding of any kind or nature in any court in which an action may be commenced arising out of this Loan Agreement or by reason of any other cause or dispute whatsoever between them. The parties hereto agree that the state and federal Courts which sit in the State of California and the County of Orange shall have exclusive jurisdiction to hear and determine any claims or disputes between Borrower and Lender, pertaining directly or indirectly to this Loan Agreement or to any matter arising therefrom. The parties each expressly submit and consent in advance to such jurisdiction in any action or proceeding commenced in such courts provided that such consent shall not be deemed to be a waiver of personal service of the summons and complaint, or other process or papers issued therein. The choice of forum set forth in this Section 11.9 shall not be deemed to preclude the enforcement of any judgment obtained in such forum or the taking of any action under this Loan Agreement to enforce same in any appropriate jurisdiction. The parties each waive any objection based upon forum non conveniens and any objection to venue of any action instituted hereunder.

12.12 Confidentiality. Lender and Borrower shall:

(a) not disclose any Confidential Information of the other to third parties except to: (i) government authorities; or (ii) such party's Affiliates, consultants or actual or potential contract manufacturers, licensees, distributors, purchasers, joint ventures, clinical investigators or other persons having bona fide business relations with such party, in each case pursuant to a non-disclosure commitment; and

(b) take such precautions as it normally takes with its own confidential and proprietary information to prevent disclosure to third parties of any Confidential Information (except as contemplated above);

provided, however, that no party shall be obligated to maintain confidentiality under this Section 12.12 with respect to any information that (A) at the time of disclosure is or thereafter becomes available to the general public other than by breach of this Section 12.12 by such party; (B) is obtained by such party from a third-party source who is not breaching a commitment of confidentiality to the other party to this Loan Agreement by disclosing such information to such first party; or (C) is required to be disclosed pursuant to law to protect such party's interest or in connection with any litigation, investigation or regulatory proceeding, or as otherwise required by law.

12.13 Titles and Subtitles. The titles of the articles, sections and subsections of this Loan Agreement are for convenience of reference only and are not to be considered in construing this Loan Agreement.

12.14 Counterparts. This Agreement may be executed in any number of counterparts, each of which shall be an original, but all of which together shall constitute one instrument.

IN WITNESS WHEREOF, Borrower and Lender have caused this Loan Agreement to be duly executed by their duly authorized officers all as of the day and year first above written.

"BORROWER"

"LENDER"

HALSEY DRUG CO., INC.

WATSON PHARMACEUTICALS, INC.

/s/ Michael Reicher

/s/ Robert C. Funsten

By:

By:

Its: Chief Executive Officer

Its: Senior Vice President

SCHEDULE I

HOLDERS OF EXISTING DEBENTURES RECEIVING IN-KIND INTEREST PAYMENTS

ORACLE STRATEGIC PARTNERS, L.P.

GALEN PARTNERS III, L.P.

GALEN EMPLOYEE FUND III, L.P.

GALEN PARTNERS INTERNATIONAL, III, L.P.

MICHAEL REICHER

PETER CLEMENS

AMENDMENT

TO

LOAN AGREEMENT

This AMENDMENT TO LOAN AGREEMENT, dated as of March 31, 2000 (the "Amendment"), is made and entered into by and between Halsey Drug Co., Inc., a New York corporation ("Borrower"), and Watson Pharmaceuticals, Inc., a Nevada corporation ("Lender"). Capitalized terms used herein shall have the meanings given them in the Loan Agreement (as defined below).

Recitals

WHEREAS, Borrower and Lender are parties to that certain Loan Agreement, dated as of March 29, 2000 (the "Loan Agreement"); and

WHEREAS, Borrower and Lender desire to amend certain terms of the Loan Agreement;

NOW, THEREFORE, the parties hereto agree as follows.

Agreement

1. Article One of the Loan Agreement is hereby amended in its entirety to read as follows:

"1. AMOUNT AND TERMS OF LOAN.

1.1 Term Loans. Subject to the terms herein, Lender agrees to loan to Borrower from time to time the aggregate principal amount of Seventeen Million Five Hundred Thousand Dollars (\$17,500,000) (such take-downs, individually and collectively, the "Loan"). Borrower may request take-downs of the Loan hereunder upon five Business Days' written notice, such notice to be accompanied by a statement of uses of proceeds of past take-downs, if any, and proposed uses of proceeds of the take-down being requested. Such statement is for informational purposes only. Notwithstanding any prepayment of the Loan by Borrower, sums repaid hereunder may not be re-borrowed.

1.2 Promissory Note. Borrower's obligation to pay the principal of, and interest on, the Loan shall be evidenced by a secured promissory note (the "Note"), duly executed and delivered by Borrower, such Note to be in the form attached as Exhibit A to the Amendment to this Loan Agreement, dated March 31, 2000, by and between Borrower and Lender."

2. Limitation of Amendment. Except as amended above, the terms of the Loan Agreement shall remain in full force and effect.

3. Governing Law. This Amendment and the rights of the parties hereunder shall be governed in all respects by the laws of the State of California wherein the terms of this Amendment were negotiated.

4. Counterparts. This Amendment may be executed in any number of counterparts, each of which shall be an original, but all of which together shall constitute one instrument.

IN WITNESS WHEREOF, Borrower and Lender have caused this Amendment to be duly executed by their duly authorized officers all as of the day and year first above written.

"BORROWER"

"LENDER"

HALSEY DRUG CO., INC.

WATSON PHARMACEUTICALS, INC.

/s/ Michael Reicher

/s/ Robert C. Funsten

By:

By:

Its: Chief Executive Officer

Its: Senior Vice President

SECURED PROMISSORY NOTE

\$17,500,000.00

March 31, 2000
Corona, California

1. Promise to Pay. For good and valuable consideration, the receipt of which is hereby acknowledged, HALSEY DRUG CO., INC., a New York corporation, ("Maker"), promises to pay to WATSON PHARMACEUTICALS, INC., a Nevada corporation ("Watson"), or order (either, the "Holder"), on the Maturity Date (as defined below), unless sooner paid as provided in Section 4 hereof, the principal sum of Seventeen Million Five Hundred Thousand Dollars (\$17,500,000.00), plus accrued unpaid interest thereon. The outstanding principal balance of this Note shall bear interest at a variable rate equal to the prime rate announced from time to time by Bank of America (the "Prime Rate") plus two percent (2.0%) per annum (the "Interest Rate") from the date such principal amount becomes outstanding to the date the principal sum is paid in full; provided, however, that if this Note is not paid in full on the Maturity Date, the unpaid balance of the Note shall bear interest therefrom and until paid at the Default Rate (as defined below). Payments of interest shall be due on the each March 31, June 30, September 30 and December 31 during the term of this Note commencing June 30, 2000. All payments under this Note shall be made to the order of the Holder at 311 Bonnie Circle, Corona, California, 92880, or such other address as Holder may designate in writing to Maker, in U.S. dollars, and shall be applied first to accrued unpaid interest, if any, and then to principal.

2. Maturity Date. The date that this Note shall mature, and the principal amount outstanding hereunder, plus accrued unpaid interest thereon and any charges pertaining thereto, shall become due and payable (the "Maturity Date") shall be March 31, 2003.

3. Loan and Security Agreements. Maker and Watson are party to that certain Loan Agreement, dated as of even date herewith (the "Loan Agreement"), pursuant to which this Note is being issued. The full and punctual payment and performance of this Note by Maker are secured and guaranteed by the Company General Security Agreement, the Company Collateral Assignments, the Stock Pledge Agreement, the Guaranties, the Guarantors Security Agreement, the Guarantor Collateral Assignments and the Mortgage, as those terms are defined in the Loan Agreement (the "Security Agreements"). The security interest granted to Holder under the Security Agreements extends to the proceeds of any sale or other transfer or disposition of such assets, whether by Maker, its affiliates, the Holder or any other person, that occurs prior to the payment in full of this Note. Copies of the Loan Agreement and the Security Agreements may be obtained from Maker without charge.

4. Prepayments. Maker may voluntarily prepay this Note either in whole or in part without penalty or premium.

5. Waivers. Maker hereby waives diligence, presentment for payment, demand, protest, notice of non-payment, notice of dishonor, notice of protest, and any and all other notices and demands whatsoever. Maker shall remain bound under this Note until all principal and interest and any other amounts that are payable hereunder or under the Loan Agreement or the Security Agreements have been paid in full, notwithstanding any extensions or renewals granted with respect to this Note or the release of any party liable hereunder or any security for the payment of this Note. Maker, and any and all endorser hereof, also waive the right to plead any and all statutes of limitations as a defense to any demand on this Note or any and all obligations or liabilities arising out of or in connection with this Note, the Loan Agreement or the Security Agreements, to the fullest extent permitted by law.

6. Events of Default. Any of the following events shall constitute an event of default by Maker under this Note (an "Event of Default"):

(a) the failure of Maker to pay to Holder, on the Maturity Date, any and all principal amounts due and owing under this Note;

(b) the failure of maker to pay to Holder interest payments when due;

or

(c) there occurs any other event or circumstance that constitutes an "Event of Default" as defined in Section 8.1 of the Loan Agreement.

Upon the occurrence of any Event of Default, as defined hereinabove, at Holder's option, Holder may declare immediately due and payable, and on any such declaration there shall become immediately due and payable, the entire unpaid principal balance of this Note, together with all accrued and unpaid interest under this Note and any other sums owing at the time of such declaration pursuant to this Note, the Loan Agreement or the Security Agreements, and Holder shall be entitled to exercise all rights and remedies available to Holder under this Note, under the Loan Agreement and the Security Agreements and under applicable law, all of which rights and remedies shall be cumulative. Without limiting the generality of the foregoing, upon the occurrence of an Event of Default, the interest rate at which interest shall accrue on the principal sum and any other amounts that are due under this Note shall increase to the lower of (i) the Prime Rate plus four percent (4.0%) per annum or (ii) the maximum interest rate permitted under applicable law (the "Default Rate"), until all such amounts have been paid in full.

7. No Waiver by Holder. Any delay or omission on the part of Holder to exercise any of Holder's rights or remedies hereunder, under the Loan Agreement or the Security Agreements or under applicable law, including, without limitation, the right to accelerate amounts owing under this Note, shall not be deemed a waiver of that right or remedy or of any other right or remedy of Holder in respect thereof. The acceptance by Holder of any payment pursuant to the terms of this Note which is less than payment in full of all amounts due and payable at the time of such payment shall not constitute a waiver of the right to exercise any of the Holder's rights or remedies under this Note, the Loan Agreement, the Security Agreements or under applicable law at that time or at any subsequent time or nullify any prior exercise of any such rights or remedies without the express written consent of Holder, except as and to the extent provided to the contrary by applicable law.

8. Governing Law. This Note shall be governed by and construed according to and enforced under the internal laws of the State of California without giving effect to its choice of laws rules.

9. Enforcement of the Note. Maker agrees that the Superior Court in and for the County of Orange, California shall have exclusive jurisdiction over any disputes, between the Maker and Holder and any action, suit or other proceeding brought by Maker or Holder relating to the interpretation or enforcement of this Note, and Maker agrees as follows: (a) Maker shall accept and not contest the personal or subject matter jurisdiction of such Court; (b) Maker shall accept and not object to or challenge the venue of such Court or assert the doctrine of forum non conveniens with respect to such Court; (c) Maker shall accept and not contest the validity or effectiveness of service of process in any such action, suit or other proceeding by registered or certified first class mail; and (d) TO THE MAXIMUM EXTENT PERMITTED BY LAW, MAKER WAIVES AND SHALL WAIVE ANY RIGHT TO A TRIAL BY JURY IN ANY ACTION OR OTHER PROCEEDING BROUGHT WITH RESPECT TO THIS NOTE OR ITS ENFORCEMENT OR INTERPRETATION. If Maker fails to pay any amounts due hereunder when due, or if an Event of Default occurs, then Maker shall pay all costs of enforcement and collection, including, without limitation, reasonable attorneys' fees and costs incurred by Holder, whether or not enforcement and collection includes the filing of a lawsuit, and whether or not that lawsuit is prosecuted to judgment. The costs of enforcement and collection shall be added to the principal amount of the Note and shall accrue interest at the Default Rate from the date incurred by Holder to the date paid by Maker.

10. Binding Nature. The provisions of this Note shall be binding on Maker and shall inure to the benefit of the Holder.

11. Usury Savings Provisions. In the event Holder receives any sums under this Note which constitute interest in an amount in excess of that permitted by any applicable law, then, all such sums constituting interest in excess of that permitted to be paid under applicable law shall, at Holder's option, either be credited to the payment of principal owing hereunder or returned to Maker. The provisions of this Section 11 control the other provisions of this Note and any other agreement between Maker and Holder.

12. Severability. If, but only to the extent that, any provision of this Note shall be invalid or unenforceable, then, such offending provision shall be deleted from this Note, but only to the extent necessary to preserve the validity and effectiveness of this Note to the fullest extent permitted by applicable law.

13. Interpretation. No provision of this Note shall be interpreted for or against Maker or Holder because that person or that person's legal representative drafted such provision. Unless otherwise indicated elsewhere in this Note, (a) the term "or" shall not be exclusive, (b) the term "including" shall mean "including, but not limited to," and (c) the terms "below," "above," "herein," "hereof," "hereto," "hereunder" and other terms similar to such terms shall refer to this Note as a whole and not merely to the specific section, subsection, paragraph or clause where such terms may appear. The section and sub-section headings in this Note are included for convenience of reference only and shall be ignored in the construction or interpretation of this Note.

"MAKER"

HALSEY DRUG CO., INC.

/s/ Michael Reicher

By:

Its: Chief Executive Officer

WATSON SECURITY AGREEMENT

THIS WATSON SECURITY AGREEMENT ("Security Agreement") is made and entered into as of March 29, 2000, by and between HALSEY DRUG CO., INC., a New York corporation ("Borrower"), and WATSON PHARMACEUTICALS, INC., a Nevada corporation ("Lender").

W I T N E S S E T H

WHEREAS, Borrower and Lender have entered into that certain Loan Agreement dated as of the date hereof (as the same may be amended, modified, supplemented or restated from time to time, the "Loan Agreement"; terms which are capitalized herein and not otherwise defined shall have the meanings ascribed to them in the Loan Agreement); and

WHEREAS, Lender requires, as a condition precedent to the effectiveness of the Loan Agreement, that Borrower (i) grant to Lender a first priority lien on all the real and personal property and assets of Borrower, now existing or hereinafter acquired (as defined in Section II below, the "Collateral") and (ii) execute and deliver the Security Agreement in order to secure the payment and performance by Borrower of the Obligations.

NOW, THEREFORE, in order to induce Lender to enter into and perform the Loan Agreement and as consideration for Lender entering into and performing such, Borrower hereby agrees as follows:

SECTION I

CREATION OF SECURITY INTEREST

Borrower hereby pledges, assigns and grants to Lender a continuing perfected first priority lien on and security interest in all of Borrower's right, title and interest in and to the Collateral (as defined in Section II below) in order to secure the payment and performance of all Obligations owing by Borrower to Lender.

SECTION II

COLLATERAL

For purposes of this Security Agreement, the term "Collateral" shall mean, with respect to Borrower, all of the kinds and types of real and personal property described in subsections A through F hereof, whether now owned or hereafter at any time arising, acquired or created by Borrower and wherever located, including all replacements, additions, accessions, substitutions, repairs, proceeds and products relating thereto or therefrom, and all documents, ledger sheets and files of Borrower relating thereto. "Proceeds" hereunder include (i) whatever is now or hereafter received by Borrower upon the sale, exchange, collection or other disposition of any item of Collateral, whether such proceeds constitute inventory, accounts, accounts receivable, general intangibles, instruments, securities (including, without limitation, United States of America Treasury Bills), credits, claims, demands, documents, letters of credit and letter of credit proceeds, chattel paper, documents of title, certificates of title, certificates of deposit, warehouse receipts, bills of lading, leases, deposit accounts, money, tax refund claims, contract rights, goods or equipment and

(ii) any such items which are now or hereafter acquired by Borrower with any proceeds of Collateral hereunder:

A. Accounts. All of Borrower's accounts, whether now existing or existing in the future, including without limitation (i) all accounts receivable (whether or not specifically listed on schedules furnished to lender), including, without limitation, all accounts created by or arising from all of Borrower's sales of goods or rendition of services made under any of Borrower's trade names, or through any of its divisions, (ii) all the unpaid sellers' rights (including rescission, repletion, reclamation and stoppage in transit) relating to the foregoing or arising therefrom, (iii) all rights to any goods represented by any of the foregoing, including returned or repossessed goods, (iv) all reserves and credit balances held by Borrower with respect to any such accounts receivable or account debtors and (v) all guarantees or collateral for any of the foregoing (all of the foregoing property and similar property being hereinafter referred to as "Accounts");

B. Inventory. All of Borrower's inventory, including without limitation (i) all raw materials, work in progress, parts, components, assemblies, supplies and materials used or consumed in Borrower's businesses, wherever located and whether in the possession of Borrower or any other Person (for the purposes of the Security Agreement, the term "Person" means any individual, sole proprietorship, partnership, joint venture, trust, unincorporated organization, association, corporation, institution, entity, party or government, including any division, agency or department thereof); (ii) all goods, wares and merchandise, finished or unfinished, held for sale or lease or leased or furnished or to be furnished under contracts of service, wherever located and whether in the possession of Borrower or any other Person or entity; and (iii) all goods returned to or repossessed by Borrower (all of the foregoing property being hereinafter referred to as "Inventory");

C. Equipment. All of the equipment owned or leased by Borrower, including, without limitation, machinery, equipment, office equipment and supplies, computers and related equipment, furniture, furnishings, tools, tooling, jigs, dies, fixtures, manufacturing implements, fork lifts, trucks, trailers, motor vehicles, and other equipment (all of the foregoing property being hereinafter referred to as "Equipment");

D. Intangibles. All of Borrower's general intangibles, instruments, securities (including without limitation United States of America Treasury Bills), credits, claims, demands, documents, letters of credit and letter of credit proceeds, chattel paper, documents of title, certificates of title, certificates of deposit, warehouse receipts, bills of lading, leases which are permitted to be assigned or pledged, deposit accounts, money, tax refund claims, contract rights which are permitted to be assigned or pledged (all of the foregoing property being hereinafter referred to as "Intangibles"); and

E. Intellectual Property. All of Borrower's intellectual property, including, without limitation, New Drug Applications, Investigatory New Drug Applications, Abbreviated New Drug Applications, Alternative New Drug Applications, registrations and quotas as issued by the Drug Enforcement Administration and/or the Attorney General of the United States pursuant to the Controlled Substances Act, certifications, permits and approvals of federal and state governmental agencies, patents, patent applications, trademarks, trademark applications, service marks, service mark applications, trade names, technical knowledge and processes, formal or informal licensing arrangements which are permitted to be assigned or pledged, blueprints, technical specifications, computer software, copyrights, copyright applications and other trade secrets, and all embodiments thereof, and rights thereto, including, without limitation, all of Borrower rights to use the patents, trademarks, copyrights, service marks, or other property of the aforesaid nature of other Persons now

or hereafter licensed to Borrower, together with the goodwill of the business symbolized by or connected with Borrower's trademarks, copyrights, service marks, licenses and the other rights included in this section II (E).

F. Real Property. All of Borrower's right, title and interest to real property, including, without limitation, Borrower's right, title and interest to the Brooklyn Facility Lease and the Congers Facility Lease.

SECTION III

BORROWER'S REPRESENTATIONS AND WARRANTIES

Borrower represents and warrants as follows:

A. Places of Business. Borrower has no places of business, or warehouses in which it leases space, other than those set forth on Section III A. of Schedule A, a copy of which is attached hereto and made a part hereof ("Schedule A").

B. Location of Collateral. Except for the movement of Collateral from time to time from one place of business or warehouse listed on Section III A. of Schedule A to another place of business or warehouse listed on Section III A. of such Schedule A, the Collateral is located at Borrower's chief executive offices or other places of business or warehouses listed on such Section III A. of Schedule A, and not at any other location.

C. Restrictions on Collateral Disposition. Except as otherwise provided in the Loan Agreement, none of the Collateral is subject to contractual obligations that may restrict or inhibit Lender's rights or ability to sell or dispose of the Collateral or any part thereof after the occurrence of an Event of Default.

D. Status of Accounts. Each Account is based on an actual and bona fide rendition of services to customers, made by Borrower in the ordinary course of its business; the Accounts created are its exclusive property and are not and shall not be subject to any lien, consignment arrangement, encumbrance, security interest or financing statement whatsoever, except as otherwise provided in Section III D. of Schedule A, and to the best knowledge of Borrower, Borrower's customers have accepted the services, and owe and are obligated to pay the full amounts stated in the invoices according to their terms, without any dispute, offset, defense or counterclaim.

SECTION IV

COVENANTS OF BORROWER

Borrower agrees as follows:

A. Defend Against Claims. Borrower will defend the Collateral against all claims and demands of all persons at any time claiming the same or any interest therein unless both Lender and Borrower determine that the claim or demand is not material and that, consequently, such defense would not be consistent with good business judgment. Borrower will permit any lien notices with respect to the Collateral or any portion thereof to exist or be on file in any public office except for those in favor of Lender and those permitted under the terms of the Loan Agreement.

B. Change in Collateral Location. Borrower will not (i) change its corporate name, (ii) change the location of its chief executive office or establish any place of business other than those specified in Section III A. of Schedule A, or (iii) move or permit movement of the Collateral from the locations specified therein except from one such location to another such location, unless in each case Borrower shall have given Lender at least thirty (30) days prior written notice thereof, and shall have, in advance, executed and caused to be filed and/or delivered to Lender any financing statements or other documents required by Lender to perfect the security interest of in the Collateral in accordance with Section IV C. hereof, all in form and substance satisfactory to Lender.

C. Additional Financing Statements. Promptly upon the reasonable request of Lender, Borrower will execute and deliver or use its reasonable efforts to procure any document, give any notices, execute and file any financing statements, mortgages or other documents, all in form and substance satisfactory to Lender, mark any chattel paper, deliver any chattel paper or instruments to Lender and take any other actions that are necessary or, in the opinion of Lender, desirable to perfect or continue the perfection and the first priority of Lender's security interest in the Collateral, to protect the Collateral against the rights, claims, or interests of third persons, or to effect the purposes of this Security Agreement. Borrower will pay the costs incurred in connection with any of the foregoing.

D. Additional Liens; Transfers. Without the prior written consent of Lender, Borrower will not, in any way, hypothecate or create or permit to exist any lien, security interest, charge or encumbrance on or other interest in the Collateral, other than Permitted Liens, and Borrower will not sell, transfer, assign, pledge, collaterally assign, exchange or otherwise dispose of the Collateral, other than the sale of Inventory in the ordinary course of business and the sale of obsolete or worn out Equipment. Notwithstanding the foregoing, if the proceeds of any such sale consist of notes, instruments, documents of title, letters of credit or chattel paper, such proceeds shall be promptly delivered to Lender to be held as Collateral hereunder. If the Collateral, or any part thereof, is sold, transferred, assigned, exchanged, or otherwise disposed of in violation of these provisions, the security interest of Lender shall continue in such Collateral or part thereof notwithstanding such sale, transfer, assignment, exchange or other disposition, and Borrower will hold the proceeds thereof for the benefit of Lender, and promptly transfer such proceeds to Lender in kind.

E. Contractual Obligations. Borrower will not enter into any contractual obligations which may restrict or inhibit Lender's rights or ability to sell or otherwise dispose of the Collateral or any part thereof after the occurrence or during the continuance of an Event of Default.

F. Lender's Right to Protect Collateral. Upon the occurrence or continuance of an Event of Default, Lender shall have the right at any time to make any payments and do any other acts may deem necessary to protect the security interests of Lender in the Collateral, including, without limitation, the rights to pay, purchase, contest or compromise any encumbrance, charge or lien which, in the reasonable judgment of Lender, appears to be prior to or superior to the security interests granted hereunder, and appear in and defend any action or proceeding purporting to affect its security interests in, and/or the value of, the Collateral. Borrower hereby agrees to reimburse Lender for all payments made and expenses incurred under this Security Agreement including reasonable fees, expenses and disbursements of attorneys and paralegals acting for Lender, including any of the foregoing payments under, or acts taken to protect its security interests in, the Collateral, which amounts shall be secured under this Security Agreement, and agree they shall be bound by any payment made or act taken by Lender hereunder absent Lender's gross negligence or willful

misconduct. Lender shall have no obligation to make any of the foregoing payments or perform any of the foregoing acts.

G. Further Obligations With Respect to Accounts. In furtherance of the continuing assignment and security interest in the Accounts of Borrower granted pursuant to this Security Agreement, upon the creation of Accounts, upon Lender's request, Borrower will execute and deliver to Lender in such form and manner as Lender may require, solely for its convenience in maintaining records of Collateral, such confirmatory schedules of Accounts, and other appropriate reports designating, identifying and describing the Accounts as Lender may reasonably require. In addition, upon Lender's request, Borrower shall provide Lender with copies of agreements with, or purchase orders from, the customers of Borrower and copies of invoices to customers, proof of shipment or delivery and such other documentation and information relating to said Accounts and other Collateral as Lender may reasonably require. Furthermore, upon Lender's request, Borrower shall deliver to Lender any documents or certificates of title issued with respect to any property included in the Collateral, and any promissory notes, letters of credit or instruments related to or otherwise in connection with any property included in the Collateral, which in any such case came into the possession of Borrower, or shall cause the issuer thereof to deliver any of the same directly to Lender, in each case with any necessary endorsements in favor of Lender. Failure to provide Lender with any of the foregoing shall in no way affect, diminish, modify or otherwise limit the security interests granted herein. Borrower hereby authorizes Lender to regard Borrower's printed name or rubber stamp signature on assignment schedules or invoices as the equivalent of a manual signature by Borrower's authorized officers or agents.

H. Insurance. Borrower agrees to maintain public liability insurance, third party property damage insurance and replacement value insurance on the Collateral under such policies of insurance, with such insurance companies, in such amounts and covering such risks as are at all times satisfactory to Lender in its commercially reasonable judgment. All policies covering the Collateral are to name Lender as an additional insured and the loss payee in case of loss, and are to contain such other provisions as Lender may reasonably require to fully protect Lender's interest in the Collateral and to any payments to be made under such policies.

I. Taxes. Borrower agrees to pay, when due, all taxes lawfully levied or assessed against Borrower or any of the Collateral before any penalty or interest accrues thereon; provided, however, that, unless such taxes have become a Federal tax or Employment Retirement Security Income Act lien on any of the assets of Borrower, no such tax need be paid if the same is being contested, in good faith, by appropriate proceedings promptly instituted and diligently conducted and if an adequate reserve or other appropriate provision shall have been made therefor as required in order to be in conformity with generally accepted accounting principles and procedures in effect in the United States of America.

J. Compliance with Laws. Borrower agrees to comply in all material respects with all requirements of law applicable to the Collateral or any part thereof, or to the operation of its business or its assets generally, unless Borrower contests any such requirements of law in a reasonable manner and in good faith. Borrower agrees to maintain in full force and effect, its respective licenses and permits granted by any governmental authority as may be necessary or advisable for Borrower to conduct its business in all material respects.

K. Maintenance of Property. Borrower agrees to keep all property useful and necessary to its business in good working order and condition (ordinary wear and tear excepted) and not to commit or suffer any waste with respect to any of their properties.

L. Environmental and Other Matters. Borrower will conduct its business so as to comply in all material respects with all environmental, land use, occupational, safety or health laws, regulations, directions, ordinances, criteria and guidelines in all jurisdictions in which it is or may at any time be doing business, except to the extent that Borrower is contesting, in good faith by appropriate legal, administrative or other proceedings, any such law, regulation, direction, ordinance, criteria, guideline, or interpretation thereof or application thereof; provided, further, that Borrower shall comply with the order of any court or other governmental authority relating to such laws unless Borrower shall currently be prosecuting an appeal, proceedings for review or administrative proceedings and shall have secured a stay of enforcement or execution or other arrangement postponing enforcement or execution pending such appeal, proceedings for review or administrative proceedings.

M. Further Assurances. Borrower shall take all such further actions and execute all such further documents and instruments (including, but not limited to, collateral assignments of Intellectual Property and Intangibles or any portion thereof) as Lender may at any time reasonably determine in its sole discretion to be necessary or desirable to further carry out and consummate the transactions contemplated by the Loan Agreement and the documentation relating thereto, including the Security Agreement, and to perfect or protect the liens (and the priority status thereof) of Lender in the Collateral.

SECTION V

REMEDIES

A. Obtaining the Collateral Upon Default. If any Event of Default shall have occurred and be continuing, then and in every such case, subject to any mandatory requirements of applicable law then in effect, Lender, in addition to any rights now or hereafter existing under applicable law, shall have all rights as a secured creditor under the Uniform Commercial Code in all relevant jurisdictions and may:

(a) personally, or by agents or attorneys, immediately retake possession of the Collateral or any part thereof, from Borrower or any other Person who then has possession of any part thereof, with or without notice or process of law, and for that purpose may enter upon Borrower's premises where any of the Collateral is located and remove the same and use in connection with such removal any and all services, supplies, aids and other facilities of Borrower;

(b) instruct the obligor or obligors on any agreement, instrument or other obligation (including, without limitation, the Accounts) constituting the Collateral to make any payment required by the terms of such instrument or agreement directly to Lender;

(c) withdraw all monies, securities and instruments held pursuant to any pledge arrangement for application to the Obligations;

(d) sell, assign or otherwise liquidate, or direct Borrower to sell, assign or otherwise liquidate, any or all of the Collateral or any part thereof, and take possession of the proceeds of any such sale or liquidation;

(e) take possession of the Collateral or any part thereof, by directing Borrower in writing to deliver the same to Lender at any place or places designated by Lender, in which event Borrower shall at its own expense:

(i) forthwith cause the same to be moved to the place or places so designated by Lender and there delivered to Lender,

(ii) store and keep any Collateral so delivered to Lender at such place or places pending further action by Lender as provided in Section V B., and

(iii) while the Collateral shall be so stored and kept, provide such guards and maintenance services as shall be necessary to protect the same and to preserve and maintain the Collateral in good condition; it being understood that Borrower's obligation to so deliver the Collateral is of the essence of this Security Agreement and that, accordingly, upon application to a court of equity having jurisdiction, Lender shall be entitled to a decree requiring specific performance by Borrower of said obligation.

B. Disposition of the Collateral. Any collateral repossessed by Lender under or pursuant to Section V A. and any other Collateral whether or not so repossessed by Lender, may be sold, assigned, leased or otherwise disposed of under one or more contracts or as an entirety, and without the necessity of gathering at the place of sale the property to be sold, and in general in such manner, at such time or times, at such place or places and on such terms as Lender may, in compliance with any mandatory requirements of applicable law, determine to be commercially reasonable. Any of the Collateral may be sold, leased or otherwise disposed of, in the condition in which the same existed when taken by Lender or after any overhaul or repair which Lender shall determine to be commercially reasonable. Any such disposition which shall be a private sale or other private proceedings permitted by such requirements shall be made upon not less than ten (10) days' written notice to Borrower specifying the time at which such disposition is to be made and the intended sale price or other consideration therefor, and shall be subject, for the ten (10) days after the giving of such notice, to the right of Borrower or any nominee of Borrower to acquire the Collateral involved at a price or for such other consideration at least equal to the intended sale price or other consideration so specified. Any such disposition which shall be a public sale permitted by such requirements shall be made upon not less than ten (10) days' written notice to Borrower specifying the time and place of such sale and, in the absence of applicable requirements of law, shall be by public auction (which may, at the option of Lender, be subject to reserve), after publication of notice of such auction not less than ten (10) days prior thereto in two (2) newspapers in general circulation in the City of New York as Lender may determine. To the extent permitted by any such requirement of law, Lender may bid for and become the purchaser of the Collateral or any item thereof, offered for sale in accordance with this Section without accountability to Borrower (except to the extent of surplus money received). If, under mandatory requirements of applicable law, Lender shall be required to make disposition of the Collateral within a period of time which does not permit the giving of notice to Borrower as herein above specified, Lender need give Borrower only such notice of disposition as shall be reasonably practicable in view of such mandatory requirements of applicable law.

C. Power of Attorney. Borrower hereby irrevocably authorizes and appoints Lender, or any Person that Lender may designate, as Borrower's attorney-in-fact, at Borrower's cost and expense, to exercise all of the following powers upon and at any time after the occurrence and during the continuance of an Event of Default, which powers, being coupled with an interest, shall be irrevocable until all of the Obligations owing by Borrower shall have been paid and satisfied in full:

(a) accelerate or extend the time of payment, compromise, issue credits, bring suit or administer and otherwise collect Accounts or proceeds of any Collateral;

(b) receive, open and dispose of all mail addressed to Borrower and notify postal authorities to change the address for delivery thereof to such address as Lender may designate;

(c) give customers indebted on Accounts notice of Lender's interest therein, and/or to instruct such customers to make payment directly to Lender for Borrower's account;

(d) convey any item of Collateral to any purchaser thereof;

(e) give any notices or record any liens under Section IV C. hereof; and

(f) make any payments or take any acts under Section IV F. hereof.

Lender's authority under this Section V C. shall include, without limitation, the authority to execute and give receipt for any certificate of ownership or any document, transfer title to any item of Collateral, sign Borrower's name on all financing statements or any other documents deemed necessary or appropriate to preserve, protect or perfect the security interest in the Collateral and to file the same, prepare, file and sign Borrower's name on any notice of lien, assignment or satisfaction of lien or similar document in connection with any Account and prepare, file and sign Borrower's name on a proof of claim in bankruptcy or similar document against any customer of Borrower, and to take any other actions arising from or incident to the rights, powers and remedies granted to Lender in this Security Agreement. This power of attorney is coupled with an interest and is irrevocable by Borrower.

D. Waiver of Claims. Except as otherwise provided in this Security Agreement, BORROWER HEREBY WAIVES, TO THE EXTENT PERMITTED BY APPLICABLE LAW, NOTICE AND JUDICIAL HEARING IN CONNECTION WITH LENDER'S TAKING POSSESSION OF OR DISPOSING OF ANY OF THE COLLATERAL, INCLUDING, WITHOUT LIMITATION, ANY AND ALL PRIOR NOTICE AND HEARING FOR ANY PREJUDGMENT REMEDY OR REMEDIES AND ANY SUCH RIGHT WHICH BORROWER WOULD OTHERWISE HAVE UNDER THE CONSTITUTION OR ANY STATUTE OF THE UNITED STATES OR OF ANY STATE, and Borrower hereby further waives, to the extent permitted by law:

(a) all damages occasioned by such taking of possession except any damages which are the direct result of Lender's gross negligence or willful misconduct;

(b) all other requirements as to the time, place and terms of sale or other requirements with respect to the enforcement of Lender's rights hereunder, except as expressly provided herein; and

(c) all rights of redemption, appraisalment, valuation, stay, extension or moratorium now or hereafter in force under any applicable law in order to prevent or delay the

enforcement of this Security Agreement or the absolute sale of the Collateral or any portion thereof, and Borrower, for itself and all who may claim under it, insofar as it or they now or hereafter lawfully may, hereby waives the benefit of all such laws.

Any sale of, or the grant of options to purchase, or any other realization upon any Collateral shall operate to divest all right, title, interest, claim and demand, either at law or in equity, of Borrower therein and thereto, and shall be a perpetual bar both at law and in equity against Borrower and against any and all persons claiming or attempting to claim the Collateral so sold, optioned or realized upon, or any part thereof, from, through and under Borrower.

E. Remedies Cumulative. Each and every right, power and remedy hereby specifically given to Lender shall be in addition to every other right, power and remedy specifically given under this Security Agreement, under the Loan Agreement or under other documentation relating thereto or now or hereafter existing at law or in equity, or by statute, and each and every right, power and remedy whether specifically herein given or otherwise existing may be exercised from time to time or simultaneously and as often and in such order as may be deemed expedient by Lender. All such rights, powers and remedies shall be cumulative and the exercise or the beginning of exercise of one shall not be deemed a waiver of the right to exercise of any other or others. No delay or omission of Lender in the exercise of any such right, power or remedy and no renewal or extension of any of the Obligations shall impair any such right, power or remedy or shall be construed to be a waiver of any Default or Event of Default or any acquiescence therein.

SECTION VI

MISCELLANEOUS PROVISIONS

A. Notices. All notices, approvals, consents or other communications required or desired to be given hereunder shall be delivered in person, by facsimile transmission followed promptly by first class mail or by overnight mail, and delivered if to Borrower, then to the attention of Mr. Michael Reicher, c/o Halsey Drug. Co., Inc., 695 No. Perryville Road, Rockford, Illinois, 61107, fax no. (815) 399-9710, with a copy to John P. Reilly, Esq., c/o St. John & Wayne, L.L.C., 2 Penn Plaza East, Newark, New Jersey 07105, fax no. (973) 491-3407, and if to Lender, then to the attention of the Chief Financial Officer, c/o Watson Pharmaceuticals, Inc., 311 Bonnie Circle, Corona, California, 92880, fax no. (909) 279-8094 (courtesy copy to Robert Funsten, Esq., General Counsel), with a copy to Lawrence B. Cohn, c/o Stradling Yocca Carlson & Rauth, 660 Newport Center Drive, Newport Beach, CA 92660, fax no. (949) 725-4100.

B. Headings. The headings in this Security Agreement are for purposes of reference only and shall not affect the meaning or construction of any provision of this Security Agreement.

C. Severability. The provisions of this Security Agreement are severable, and if any clause or provision shall be held invalid or unenforceable in whole or in part in any jurisdiction, then such invalidity or unenforceability shall affect, in that jurisdiction only, such clause or provision, or part thereof, and shall not in any manner affect such clause or provision in any other jurisdiction or any other clause or provision of the Security Agreement in any jurisdiction.

D. Amendments, Waivers and Consents. Any amendment or waiver of any provision of the Security Agreement and any consent to any departure by Borrower from any provision of the Security Agreement shall be effective only if made or given in writing signed by Lender.

E. Interpretation of Agreement. Time is of the essence in each provision of this Security Agreement of which time is an element. All terms not defined herein shall have the meaning set forth in the applicable Uniform Commercial Code. Acceptance of or acquiescence in a course of performance rendered under the Security Agreement shall not be relevant in determining the meaning of the Security Agreement even though the accepting or acquiescing party had knowledge of the nature of the performance and opportunity for objection.

F. Continuing Security Interest. The Security Agreement shall create a continuing security interest in the Collateral and shall (i) remain in full force and effect until indefeasible payment in full of the Obligations owing by Borrower, (ii) be binding upon Borrower, and its successors and assigns and (iii) inure to the benefit of Lender and its successors and assigns.

G. Reinstatement. To the extent permitted by law, the Security Agreement shall continue to be effective or be reinstated if at any time any amount received by Lender in respect of the Obligations owing by Borrower is rescinded or must otherwise be restored or returned by Lender upon the occurrence or during the pendency of any Event of Default, all as though such payments had not been made.

H. Survival of Provisions. All representations, warranties and covenants of Borrower contained herein shall survive the execution and delivery of this Security Agreement, and shall terminate only upon the full and final indefeasible payment and performance by Borrower of the Obligations secured hereby.

I. Setoff. Lender shall have all rights of setoff available at law or in equity.

J. Power of Attorney. In addition to the powers granted to Lender under Section V C., Borrower hereby irrevocably authorizes and appoints Lender, or any Person that Lender may designate, as Borrower's attorney-in-fact, at Borrower's cost and expense, to exercise all of the following powers, which being coupled with an interest, shall be irrevocable until all of the Obligations shall have been indefeasibly paid and satisfied in full:

(a) after the occurrence of an Event of Default, to receive, take, endorse, sign, assign and deliver, all in the name of Lender or Borrower, any and all checks, notes, drafts, and other documents or instruments relating to the Collateral; and

(b) to request, at any time from customers indebted on Accounts, verification of information concerning the Accounts and the amounts owing thereon.

K. Indemnification; Authority of Lender. Neither Lender nor any director, officer, employee, attorney or agent of Lender shall be liable to Borrower for any action taken or omitted to be taken by it or them hereunder, except for its or their own gross negligence or willful misconduct, nor shall Lender be responsible for the validity, effectiveness or sufficiency of the Security Agreement or of any document or security furnished pursuant hereto. Lender and its directors, officers, employees, attorneys and agents shall be entitled to rely on any communication, instrument or document reasonably believed by it or them to be genuine and correct and to have been signed or sent by the proper person or persons. Borrower agrees to indemnify and hold harmless Lender and any other person from and against any and all costs, expenses (including reasonable fees, expenses and disbursements of attorneys and paralegals (including, without duplication, reasonable charges of inside counsel)), claims or liability incurred by Lender or such person hereunder, unless such claim

or liability shall be due to willful misconduct or gross negligence on the part of Lender or such person.

L. Release; Termination of Agreement. Subject to the provisions of Section VI G. hereof, this Security Agreement shall terminate upon full and final indefeasible payment and performance of all the Obligations owing by Borrower. At such time, Lender shall, at the request of Borrower, reassign and redeliver to Borrower all of the Collateral hereunder which has not been sold, disposed of, retained or applied by Lender in accordance with the terms hereof. Such reassignment and redelivery shall be without warranty by or recourse to Lender, except as to the absence of any prior assignments by Lender of its interest in the Collateral, and shall be at the expense of Borrower.

M. Counterparts. The Security Agreement may be executed in one or more counterparts, each of which shall be deemed an original but all of which shall together constitute one and the same agreement.

N. GOVERNING LAW. THE VALIDITY, INTERPRETATION AND ENFORCEMENT OF THE SECURITY AGREEMENT AND ANY DISPUTE ARISING OUT OF OR IN CONNECTION WITH THIS SECURITY AGREEMENT, WHETHER SOUNDING IN CONTRACT, TORT, EQUITY OR OTHERWISE, SHALL BE GOVERNED BY THE INTERNAL LAWS (AS OPPOSED TO THE CONFLICTS OF LAWS PROVISIONS) AND DECISIONS OF THE STATE OF CALIFORNIA.

O. SUBMISSION TO JURISDICTION. ALL DISPUTES BETWEEN BORROWER AND LENDER, WHETHER SOUNDING IN CONTRACT, TORT, EQUITY OR OTHERWISE, SHALL BE RESOLVED ONLY BY STATE AND FEDERAL COURTS LOCATED IN ORANGE COUNTY, CALIFORNIA, AND THE COURTS TO WHICH AN APPEAL THEREFROM MAY BE TAKEN; PROVIDED, HOWEVER, THAT LENDER SHALL HAVE THE RIGHT, TO THE EXTENT PERMITTED BY APPLICABLE LAW, TO PROCEED AGAINST BORROWER OR ITS PROPERTY IN ANY LOCATION REASONABLY SELECTED BY LENDER IN GOOD FAITH TO ENABLE LENDER TO REALIZE ON SUCH PROPERTY, OR TO ENFORCE A JUDGMENT OR OTHER COURT ORDER IN FAVOR OF LENDER. BORROWER AGREES THAT IT WILL NOT ASSERT ANY PERMISSIVE COUNTERCLAIMS, SETOFFS OR CROSS-CLAIMS IN ANY PROCEEDING BROUGHT BY LENDER. BORROWER WAIVES ANY OBJECTION THAT IT MAY HAVE TO THE LOCATION OF THE COURT IN WHICH LENDER HAS COMMENCED A PROCEEDING, INCLUDING, WITHOUT LIMITATION, ANY OBJECTION TO THE LAYING OF VENUE OR BASED ON FORUM NON CONVENIENS.

P. SERVICE OF PROCESS. BORROWER HEREBY IRREVOCABLY AGREES THAT SERVICE OF PROCESS IN ANY LEGAL ACTION OR PROCEEDING WITH RESPECT TO THIS SECURITY AGREEMENT MAY BE EFFECTED BY MAILING A COPY THEREOF BY REGISTERED OR CERTIFIED MAIL, POSTAGE PREPAID, TO BORROWER AT ITS ADDRESS SET FORTH IN SECTION VI A. HEREOF.

Q. JURY TRIAL. BORROWER AND LENDER EACH HEREBY WAIVE ANY RIGHT TO A TRIAL BY JURY.

R. LIMITATION OF LIABILITY. LENDER SHALL NOT HAVE ANY LIABILITY TO BORROWER (WHETHER SOUNDING IN TORT, CONTRACT, OR OTHERWISE) FOR LOSSES SUFFERED BY BORROWER IN CONNECTION WITH, ARISING OUT OF, OR IN

ANY WAY RELATED TO THE TRANSACTIONS OR RELATIONSHIPS CONTEMPLATED BY THIS SECURITY AGREEMENT, OR ANY ACT, OMISSION OR EVENT OCCURRING IN CONNECTION THEREWITH, UNLESS IT IS DETERMINED BY A FINAL AND NONAPPEALABLE JUDGMENT OR COURT ORDER BINDING ON LENDER, THAT THE LOSSES WERE THE RESULT OF ACTS OR OMISSIONS CONSTITUTING GROSS NEGLIGENCE OR WILLFUL MISCONDUCT.

S. Delays; Partial Exercise of Remedies. No delay or omission of Lender to exercise any right or remedy hereunder, whether before or after the happening of any Event of Default, shall impair any such right or shall operate as a waiver thereof or as a waiver of any such Event of Default. No single or partial exercise by Lender of any right or remedy shall preclude any other or further exercise thereof, or preclude any other right or remedy.

IN WITNESS WHEREOF, Borrower has caused this Security Agreement to be duly executed and delivered as of the day and year first above written.

HALSEY DRUG CO, INC.,
a New York corporation

By: /s/ Michael Reicher
Name:
Title: Chief Executive Officer

By its acceptance hereof, as of the day and year first above written, Lender agrees to be bound by the provisions hereof applicable to it.

WATSON PHARMACEUTICALS, INC.,
a Nevada corporation

By: /s/ Robert C. Funsten
Name:
Title: Senior Vice President

WATSON STOCK PLEDGE AGREEMENT

THIS WATSON STOCK PLEDGE AGREEMENT (this "Agreement") dated as of March 29, 2000, is executed by HALSEY DRUG CO., INC., a New York corporation (the "Pledgor"), in favor of WATSON PHARMACEUTICALS, INC., a Nevada corporation (the "Pledgee").

WHEREAS, Pledgor and Pledgee have entered into that certain Loan Agreement dated as of the date hereof (as the same may be amended, modified, supplemented or restated from time to time, the "Loan Agreement"; terms which are capitalized herein and not otherwise defined shall have the meanings ascribed to them in the Loan Agreement); and

WHEREAS, it is a condition precedent to the effectiveness of the Loan Agreement that Pledgor shall have executed this Agreement and made the pledges referred to herein in favor of Pledgee.

NOW, THEREFORE, to induce Pledgee to enter into and perform the Loan Agreement and for other good and valuable consideration, the receipt and sufficiency of which are hereby acknowledged, Pledgor hereby agrees with Pledgee as follows:

1. Definitions. Unless the context otherwise requires, all terms used but not expressly defined herein shall have the meanings given to them in the Loan Agreement, or, if they are not defined in the Loan Agreement, but are defined in the California Uniform Commercial Code (the "Code"), they shall have the same meaning herein as in the Code.

2. Pledge of the Pledged Stock; Power of Attorney.

(a) As security for the prompt payment and performance when due of the Obligations, Pledgor hereby pledges and grants to Pledgee a lien on and security interest in the following (collectively the "Pledged Collateral"): (i) all of the issued and outstanding shares of common stock of each of Halsey Pharmaceuticals, Inc. ("HP, Inc." or a "Subsidiary"), Houba, Inc. ("Houba" or a "Subsidiary," and together with HP, Inc., the "Subsidiaries") which shares are more particularly described on Schedule A hereto (the "Pledged Stock"), (ii) all additional shares of common stock at any time issued to Pledgee by any of HP, Inc., and Houba, (iii) the certificates evidencing all such shares and securities, (iv) subject to Section 6 hereof, all dividends, cash, instruments and other property from time to time received, receivable or otherwise distributed in respect of or in exchange for any or all of the Pledged Stock and such shares and securities and (v) all proceeds of any of the foregoing (including, without limitation, proceeds constituting any property of the types described above). Pledgor shall deliver to Pledgee original stock certificates for all of the Pledged Stock, each accompanied by an undated stock power executed in blank by Pledgor.

(b) Pledgee shall have no obligation with respect to the Pledged Collateral or any other property held or received by it hereunder except to use reasonable care in the custody thereof to the extent required by law. Pledgee may hold the Pledged Collateral in the form in which it is received by it.

(c) Pledgor, to the full extent permitted by law, hereby constitutes and irrevocably appoints Pledgee (and any officer or agent of Pledgee, with full power of substitution and revocation) as Pledgor's true and lawful attorney-in-fact, in Pledgor's stead and in the name of Pledgor or in the name of Pledgee, to transfer, upon the occurrence and during the continuance of an

Event of Default (as hereinafter defined) or at any time Pledgee, based on all the facts and circumstances then existing, and in the exercise of its commercially reasonable credit judgment, reasonably believes in good faith, and has so notified Pledgor in writing, that, in connection with the Loan Agreement and the agreements, documents and instruments delivered by Pledgor pursuant thereto or in connection therewith, fraud has occurred with respect to Pledgor or any other Person (for the purposes of this Agreement, the term "Person" means any individual, sole proprietorship, partnership, joint venture, trust, unincorporated organization, association, corporation, institution, entity, party or government, including any division, agency or department thereof), controlling, controlled by, or under common control with Pledgor which has a material adverse effect on the operations or condition (financial or otherwise) of Pledgor and its subsidiaries, taken as a whole (a "Fraud"), the Pledged Collateral on the books of HP, Inc. and Houba, as applicable, in whole or in part, to the name of Pledgee or such other Person or Persons as Pledgee may designate and, upon the occurrence and during the continuance of an Event of Default or at any time Pledgee, based on all the facts and circumstances then existing, and in the exercise of its commercially reasonable credit judgment, reasonably believes in good faith, and has so notified Pledgor in writing, that Fraud has occurred, to take all such other and further actions as Pledgor could have taken with respect to the Pledged Collateral which Pledgee in its reasonable judgment determines to be necessary or appropriate to accomplish the purposes of this Agreement.

(d) The powers of attorney granted pursuant to this Agreement and all authority hereby conferred are granted and conferred solely to protect Pledgee's interests in the Pledged Collateral and shall not impose any duty upon the attorney-in-fact to exercise such powers. Such powers of attorney shall be irrevocable prior to the payment in full of the Obligations, and, shall not be terminated prior thereto or affected by any act of Pledgor or other Persons or by operation of law.

(e) Except to the extent that Pledgee releases its pledge of any of the Pledged Collateral, each Person who shall be a transferee of the beneficial ownership of any of Pledged Collateral shall be deemed to have irrevocably appointed Pledgee, with full power of substitution and revocation, as such Person's true and lawful attorney-in-fact in such Person's name and otherwise to do any and all acts herein permitted and to exercise any and all powers herein conferred; provided, however, no Person shall exercise any such power of attorney unless an Event of Default shall have occurred and be continuing.

3. Rights of Pledgor; Voting.

(a) During the term of this Agreement, and so long as no Voting Notice (as defined below) is received from Pledgee following the occurrence and during the continuance of an Event of Default as hereinafter provided in this Section 3, Pledgor shall have the right to vote any of the Pledged Collateral in all corporate matters except those which would contravene this Agreement, the Loan Agreement or the agreements, documents and instruments delivered by Pledgor and each Subsidiary pursuant thereto unless Pledgee consents thereto.

(b) Upon the occurrence and during the continuance of an Event of Default or from and after such time as Pledgee has notified Pledgor in writing that based on all the facts and circumstances then existing, and in the exercise of its commercially reasonable judgment, Pledgee reasonably believes in good faith that Fraud has occurred, Pledgor shall give Pledgee at least five (5) days' prior notice of (i) any meeting of stockholders of any of the Subsidiaries or any meeting of directors convened for any purpose and (ii) any written consent which Pledgor proposes to execute as the stockholder of any of the Subsidiaries or which any of the representatives of Pledgor proposes to

execute as a director of any of the Subsidiaries. During the continuance of an Event of Default, Pledgor hereby authorizes Pledgee to send its agents and representatives to any such meeting of shareholders or directors of any of one of the Subsidiaries that Pledgee wishes to attend, and agrees to take such steps as may be necessary to confirm and effectuate such authority, including, without limitation, causing such Subsidiary to give reasonable prior written notice to Pledgee of the time and place of any such meeting and the principal actions to be taken thereat.

(c) Notwithstanding the occurrence of an Event of Default, Pledgor may continue to exercise the voting rights of Pledgor as herein described (and subject to the limitations herein) except to the extent that Pledgee may elect to exercise voting power (as determined by it in its sole discretion) by a written notice given to Pledgor at any time during the continuance of an Event of Default (a "Voting Notice"), whereupon Pledgee shall have the exclusive right during the continuance of an Event of Default to exercise such rights to the extent specified in such Voting Notice, and Pledgor shall take all such steps as may be necessary to effectuate such rights until Pledgee notifies Pledgor of the release of such rights. Once any such Event of Default has been cured or waived, any relevant Voting Notice shall be deemed to be rescinded.

4. No Restrictions on Transfer. Pledgor warrants and represents that there are no restrictions on the transfer of the Pledged Stock except for such restrictions imposed by operation of law, that there are no options, warrants or rights pertaining thereto, and that Pledgor has the right to transfer Pledged Stock free of any encumbrances and without the consent of the creditors of Pledgor or the consent of any of the Subsidiaries or any other Person or any governmental agency whatsoever.

5. No Transfer or Liens; Additional Securities. Pledgor agrees that it will not sell, transfer or convey any interest in, or suffer or permit any lien or encumbrance to be created upon or with respect to, any of the Pledged Collateral during the term of this Agreement, except to or in favor of Pledgee, or as agreed to in advance by Pledgee in accordance with the terms of the Loan Agreement. Pledgor shall not cause, suffer or permit any Subsidiary to issue any common or preferred stock, or any other equity security, to any Person, unless Pledgee otherwise consents in writing (which consent may be withheld in Pledgee's reasonable credit judgment).

6. Adjustments of Capital Stock; Payment and Application of Dividends. In the event that during the term of this Agreement any stock dividend, reclassification, readjustment or other change is declared or made in the capital structure of any Subsidiary or if any other or additional shares of stock of any Subsidiary are issued to Pledgor, all new, substituted and additional shares or other securities issued by reason of any such change or acquisition shall immediately be delivered by Pledgor to Pledgee and shall be deemed to be part of the "Pledged Collateral" under the terms of this Agreement in the same manner as the shares of stock originally pledged hereunder. Upon the occurrence and during the continuance of an Event of Default, all cash dividends received by or payable to Pledgor in respect of the Pledged Collateral, including any additional shares of stock received by Pledgor as a result of Pledgor's record ownership of the Pledged Stock, shall immediately be delivered by Pledgor to Pledgee, to be held by Pledgee as Pledged Collateral hereunder or to be applied by Pledgee against the Obligations. Upon the occurrence and during the continuance of an Event of Default, Pledgor will not demand and will not be entitled to receive, any cash dividends or other income, interest or property in or with respect to the Pledged Collateral, and if Pledgor receives any of the same, Pledgor shall immediately deliver it to Pledgee to be held by it and applied as provided in the preceding sentence.

7. Warrants and Options. In the event that during the term of this Agreement subscription warrants or other rights or options shall be issued to Pledgor in connection with the Pledged Collateral, all such stock warrants, rights and options shall forthwith be assigned to Pledgee by Pledgor, and said stock warrants, rights and options shall be, and, if exercised by Pledgor, all new stock issued pursuant thereto shall be, pledged by Pledgor to Pledgee to be held as, and shall be deemed to be part of, the Pledged Collateral under the terms of this Agreement in the same manner as the shares of capital stock originally pledged hereunder.

8. Return of Pledged Collateral Upon Termination. Upon the release, satisfaction, discharge or termination of all of the Obligations and the termination of the Loan Agreement, Pledgee shall cause to be transferred or returned to Pledgor all of the stock pledged by Pledgor herein and any money, property and rights received by Pledgee pursuant hereto, to the extent Pledgee has not taken, sold or otherwise realized upon the same as permitted hereunder, together with all other documents reasonably required by Pledgor to evidence termination of the pledge contemplated hereby.

9. Events of Default; Remedies.

(a) Upon the occurrence and during the continuance of any Event of Default (as defined below), Pledgee shall have and at any time may exercise with respect to the Pledged Collateral, the proceeds thereof, and any other property or money held by Pledgee hereunder, all rights and remedies available to it under law, including, without limitation, those given, allowed or permitted to a secured party by or under the Code, and all rights and remedies provided for herein. "Event of Default" shall mean the occurrence of an Event of Default as defined in the Loan Agreement.

(b) Without limiting the foregoing, in the event that Pledgee elects to sell the Pledged Stock (such term including, for purposes of this Section 9, the Pledged Stock and all other shares of stock or securities at any time forming part of the Pledged Collateral), Pledgee shall have the power and right in connection with any such sale, exercisable at its option and in its absolute discretion, to sell, assign, and deliver the whole or any part of the Pledged Stock or any additions thereto at a private or public sale for cash, on credit or for future delivery and at such price as Pledgee deems to be satisfactory. Notice of any public sale shall be sufficient if it describes the Pledged Collateral to be sold in general terms, and is published at least once in the New York Times not less than ten (10) days prior to the date of sale. If the New York Times is not then being published, publication may be made in lieu thereof in any newspaper then being circulated in the City of New York, New York, as Pledgee may elect. All requirements of reasonable notice under this Section 9 shall be met if such notice is mailed, postage prepaid at least ten (10) days before the time of such sale or disposition, to Pledgor at its address set forth in Section 16 hereto or such other address as Pledgor may have, in writing, provided to Pledgee. Pledgee may, if it deems it reasonable, postpone or adjourn any sale of any collateral from time to time by an announcement at the time and place of the sale to be so postponed or adjourned without being required to give a new notice of sale.

(c) Because federal and state securities laws may restrict the methods of disposition of the Pledged Stock which are readily available to Pledgee, and specifically because a public sale thereof may be impossible or impracticable by reason of certain restrictions under the Securities Act of 1933, as amended, or under applicable Blue Sky or other state securities laws as now or hereafter in effect, Pledgor agrees that Pledgee may from time to time attempt to sell the Pledged Stock by means of a private placement restricting the offering or sale to a limited number of

prospective purchasers who meet suitability standards Pledgee deems appropriate and who agree that they are purchasing for their own accounts for investment and not with a view to distribution, and Pledgee's acceptance of the highest offer obtained therefrom shall be deemed to be a commercially reasonable disposition of the Pledged Stock. To the extent permitted by law, Pledgee or its assigns may purchase all or any part of the Pledged Stock and any purchaser thereof shall thereafter hold the same absolutely free from any right or claim of any kind. To the fullest extent permitted by law, Pledgee shall not be obligated to make any such sale pursuant to notice and may, without notice or publication, adjourn any public or private sale by announcement at the time and place fixed for the sale, and such sale may be held at any time or place to which the same may be adjourned. If any of the Pledged Stock is sold by Pledgee upon credit or for future delivery, Pledgee shall not be liable for the failure of the purchaser to pay for same and, in such event, Pledgee may resell such Pledged Stock and Pledgor shall continue to be liable to Pledgee for the full amount of the Obligations to the extent Pledgee does not receive full and final payment in cash therefor.

(d) Except as otherwise provided in the Loan Agreement or by applicable law, Pledgee shall have the sole right to determine the order in which Obligations shall be deemed discharged by the application of the proceeds of Pledged Stock or any other property or money held hereunder or any amount realized thereon.

10. Certain Representations and Warranties. Pledgor represents and warrants to Pledgee that: (a) All shares of Pledged Stock are fully paid, duly and properly issued, nonassessable and owned by Pledgor free and clear of any lien or encumbrance of any kind whatsoever, excepting those herein granted to Pledgee and to the Existing Holders (as described in the Loan Agreement), and Pledged Stock constitutes all of the outstanding securities of any class or kind of all of the Subsidiaries.

(a) No effective financing statement or other instrument similar in effect covering all or any part of the Pledged Collateral is on file in any recording office.

(b) The pledge of the Pledged Collateral pursuant to this Agreement creates a valid and perfected security interest in the Pledged Collateral, securing the payment of the Obligations, and all filing and other actions necessary or desirable to perfect and protect such security interest having been duly made or taken.

(c) Except as contemplated by the Loan Agreement or the Subordination Agreement, no authorization, approval or other action by, and no notice to or filing with, any governmental authority or regulatory body is required for (i) the pledge by Pledgor of the Pledged Collateral pursuant to this Agreement, the grant by Pledgor of the assignment or security interest granted hereby or the execution, delivery or performance of this Agreement by Pledgor, (ii) the perfection of or exercise by Pledgee of its rights and remedies provided for in this Agreement, or (iii) the exercise by Pledgee of the voting or other rights provided for in this Agreement or the remedies in respect of the Pledged Collateral pursuant to this Agreement (except as may be required in connection with a judicial foreclosure, if applicable, or the disposition of the Pledged Stock by laws affecting the offering and sale of securities generally).

(d) Pledgor has full right, power and authority to enter into this Agreement and to grant the security interest in the Pledged Collateral made hereby, and this Agreement constitutes the legal, valid and binding obligation of Pledgor enforceable against Pledgor in accordance with its terms, except as the enforceability thereof may be (i) limited by bankruptcy, insolvency,

reorganization, moratorium or similar laws affecting the enforceability of creditors' rights generally, and (ii) subject to general principles of equity (regardless of whether such enforceability is considered in a proceeding in equity or at law).

11. Indemnity and Expenses.

(a) Pledgor agrees to and hereby indemnifies Pledgee from and against any and all claims, damages, losses, liabilities and expenses arising out of, or in connection with, or resulting from this Agreement (including, without limitation, enforcement of this Agreement) unless resulting from or arising out of the negligence, willful misconduct or bad faith of Pledgee.

(b) Pledgor agrees promptly upon Pledgee's demand to pay or reimburse Pledgee for all reasonable expenses (including, without limitation, reasonable fees and disbursements of counsel) incurred by Pledgee in connection with (i) any modification or amendment to or waiver of any provision of this Agreement requested by Pledgor, (ii) the custody or preservation of the Pledged Collateral, (iii) any actual or attempted sale or exchange of, or any enforcement, collection, compromise or settlement respecting, the Pledged Collateral or any other property or money held hereunder or any other action taken by Pledgee hereunder reasonably necessary to enforce its rights, whether directly or as attorney-in-fact pursuant to the power of attorney herein conferred, or (iv) the failure by Pledgor to perform or observe any of the provisions hereof. All such expenses shall be deemed a part of the Obligations for all purposes of this Agreement and Pledgee may apply the Pledged Collateral or any other property or money held hereunder to payment of or reimbursement for such expenses after notice and demand to Pledgor.

12. Pledgee May Perform. If Pledgor fails to perform any agreement contained herein, Pledgee may, but shall not be obligated to, perform, or cause performance of, such agreement, and the reasonable, out-of-pocket expenses of Pledgee incurred in connection therewith shall be payable by Pledgor.

13. Waivers and Amendment. The rights and remedies given hereby are in addition to all others however arising, but it is not intended that any right or remedy be exercised in any jurisdiction in which such exercise would be prohibited by law. No action, failure to act or knowledge of Pledgee shall be deemed to constitute a waiver of any power, right or remedy hereunder, nor shall any single or partial exercise thereof preclude any further exercise thereof or the exercise of any other power, right or remedy. Any right or power of Pledgee hereunder in respect of the Pledged Collateral and any other property or money held hereunder may at the option of Pledgee be exercised as to all or any part of the same and the term the "Pledged Collateral" wherever used herein, unless the context clearly requires otherwise, shall be deemed to mean (and shall be read as) "the Pledged Collateral and any other property or money held hereunder or any part thereof." This Agreement shall not be amended nor shall any right hereunder be deemed waived except by a written agreement expressly setting forth the amendment or waiver and signed by Pledgor.

14. Continuing Security Interest; Assignments of Secured Debt. This Agreement shall create a continuing security interest in the Pledged Collateral and shall (i) remain in full force and effect until released in accordance herewith, (ii) be binding upon Pledgor, and Pledgor's successors and assigns, and upon each of the Subsidiaries, and its successors and assigns, and (iii) inure, together with the rights and remedies of Pledgee hereunder, to the benefit of Pledgee, its successors and permitted assigns. Without limiting the generality of the foregoing clause (iii), Pledgee may assign or otherwise transfer all or any portion of its rights and obligations under this Agreement to

any other person or entity, to the extent and in the manner provided in the Loan Agreement and such other person or entity shall thereupon become vested with all the benefits in respect hereof granted to Pledgee herein; Pledgee shall, however, retain all of its rights and powers with respect to any part of the Pledged Collateral not transferred. Any agent or nominee of Pledgee shall have the benefit of this Agreement as if named herein and may exercise all the rights and powers given to Pledgee hereunder.

15. GOVERNING LAW; SUITS. THIS AGREEMENT AND THE RIGHTS AND OBLIGATIONS OF PLEDGOR AND PLEDGEE HEREUNDER SHALL BE GOVERNED BY AND CONSTRUED IN ACCORDANCE WITH THE LAWS OF THE STATE OF CALIFORNIA, NOTWITHSTANDING ITS CONFLICTS OF LAW PRINCIPLES. THE PLEDGOR HEREBY IRREVOCABLY (I) CONSENTS THAT ANY SUIT, ACTION OR LEGAL PROCEEDING ARISING OUT OF OR RELATED IN ANY WAY TO THIS AGREEMENT SHALL, IF PLEDGEE SO ELECTS, BE BROUGHT AND ENFORCED IN STATE OR FEDERAL COURTS HAVING SITUS WITHIN THE COUNTY OF ORANGE, STATE OF CALIFORNIA AND (II) WAIVES ANY OBJECTION TO JURISDICTION OR VENUE IN ANY SUCH SUIT, ACTION OR PROCEEDING COMMENCED IN ANY SUCH COURT AND ANY CLAIM THAT SUCH SUIT, ACTION OR PROCEEDING HAS BEEN BROUGHT IN AN INCONVENIENT FORUM. PLEDGOR AGREES THAT SERVICE OF PROCESS IN ANY ACTION OR PROCEEDING WITH RESPECT TO THIS AGREEMENT MAY BE EFFECTED BY MAILING A COPY THEREOF BY REGISTERED OR CERTIFIED MAIL (OR ANY SUBSTANTIALLY SIMILAR FORM OF MAIL) POSTAGE PREPAID, TO PLEDGOR AT ITS ADDRESS SET FORTH IN SECTION 16 HEREOF.

16. Notices. All notices hereunder shall be in writing (except only as otherwise provided in Section 13) and shall be conclusively deemed to have been received and shall be effective (a) on the day on which delivered if delivered personally (including delivery by courier providing evidence of delivery), or transmitted by telex or telegram or telecopier with transmission confirmed, or (b) five (5) days after the date on which the same is deposited in the United States mail (certified or registered if required under Section 15), with postage prepaid and properly addressed, and any notice mailed shall be addressed:

(a) in the case of Pledgor, to:

Halsey Drug Co., Inc.
695 No. Perryville Road
Rockford, Illinois 61107

with copies to:

St. John & Wayne, L.L.C.
2 Penn Plaza East
Newark, New Jersey 07105
Attention: John P. Reilly, Esq.
Telecopier No. (973) 491-3555

(b) in the case of Pledgee, to:

Chief Financial Officer
Watson Pharmaceuticals, Inc.
311 Bonnie Circle
Corona, California 92880
Fax no. (909) 279-8094
cc: Robert Funsten, Esq.
General Counsel

with a copy to:

Stradling, Yocca, Carlson & Rauth
660 Newport Center Drive, Suite 1600
Newport Beach, CA 92660
Attention: Lawrence B. Cohn
Telecopier No. (949) 725-4100

or at such other address as the party giving such notice shall have been advised of in writing for such purpose by the party to whom or to which the same is directed.

17. WAIVERS OF JURY TRIAL AND CONSEQUENTIAL DAMAGES. THE PLEDGOR AND, BY ITS ACCEPTANCE HEREOF, PLEDGEE HEREBY WAIVE TRIAL BY JURY IN ANY LITIGATION IN ANY COURT WITH RESPECT TO, IN CONNECTION WITH, OR ARISING OUT OF THIS AGREEMENT, THE PLEDGED COLLATERAL, OR ANY INSTRUMENT OR DOCUMENT DELIVERED PURSUANT HERETO. NEITHER PLEDGOR OR PLEDGEE, NOR ANY EMPLOYEE, AGENT OR ATTORNEY OF EITHER OF THEM, SHALL BE LIABLE TO THE OTHER FOR CONSEQUENTIAL DAMAGES ARISING FROM ANY BREACH OF CONTRACT, TORT OR OTHER WRONG RELATING TO THIS AGREEMENT OR THE ESTABLISHMENT, ADMINISTRATION OR COLLECTION OF THE OBLIGATIONS, EXCEPT FOR BAD FAITH.

18. Severability: Entire Agreement.

(a) If any provision of this Agreement shall be invalid, illegal, or unenforceable in any jurisdiction, the validity, legality or enforceability of any such provision in any other jurisdiction shall not be affected or impaired, and to the extent any provision is held invalid, illegal or unenforceable, then such provision shall be deemed severable from, and shall in no way affect the validity or enforceability of the remaining provisions of this Agreement.

(b) This Agreement constitutes the entire agreement of Pledgor and replaces any other or prior agreements or undertakings, with respect to the subject matter hereof, and there are no other agreements or undertakings, oral or written, respecting such subject matter which are intended to have any force or effect after the execution hereof.

19. Miscellaneous. This Agreement shall be binding upon and shall inure to the benefit of Pledgor and Pledgee and their respective successors and permitted assigns. Section headings used herein are for convenience only and shall not affect the meaning or construction of any of the provisions hereof.

IN WITNESS WHEREOF, Pledgor has caused this Agreement to be executed by its duly authorized officer as of the day and year first above written.

HALSEY DRUG CO., INC.

By: /s/ Michael Reicher
Name:
Title: Chief Executive Officer

ACCEPTED AND AGREED TO
AS OF MARCH 29, 2000

WATSON PHARMACEUTICALS, INC.,
a Nevada corporation

By: /s/ Robert C. Funsten
Name:
Title: Senior Vice President

Each of the undersigned hereby agrees to recognize all of the rights granted to Pledgee under the foregoing Agreement and to take all actions necessary to effectuate said rights and the purposes of the Agreement including, without limitation, performance of any acts requested by Pledgee pursuant to the terms thereof.

Date: as of March 29, 2000

HALSEY PHARMACEUTICAL, INC.

By: /s/ Michael Reicher
Name:
Title: Chief Executive Officer

HOUBA, INC.

By: /s/ Michael Reicher
Name:
Title: Chief Executive Officer

SCHEDULE A

Designation and Number of
shares of capital stock owned by Pledgor

Name of Issuer Shares	Certificate No.	Designation
Halsey Pharmaceutical, Inc.	—	Common Stock, \$.01 par value
Houba, Inc.	—	Common Stock, \$.01 par value

WATSON GUARANTY

WHEREAS, HALSEY DRUG CO., INC., a New York corporation ("Borrower"), entered into a Loan Agreement dated as of March 29, 2000 (the "Loan Agreement"; terms used herein and not otherwise defined shall have the meanings given to them in the Loan Agreement), with Watson Pharmaceuticals, Inc., a Nevada Corporation ("Lender");

WHEREAS, pursuant to and in accordance with the terms of the Loan Agreement, Lender has made certain financial accommodations to Borrower and Borrower will continue to receive certain benefits from such accommodations;

WHEREAS, pursuant to and in accordance with the terms of the Loan Agreement, Lender requires that certain of Borrower's subsidiaries, Halsey Pharmaceutical, Inc., a Delaware corporation ("HP, Inc.") and Houba, Inc., an Indiana corporation (together with HP, Inc., the "Guarantors") execute and deliver this Guaranty (the "Guaranty") to Lender as a condition to the effectiveness of the Loan Agreement;

WHEREAS, the extension of credit by Lender to Borrower is necessary and desirable to the conduct and operation of the business of the Guarantors and will inure to their financial benefit; and

WHEREAS, the Guarantors are willing to guarantee the prompt payment and performance by Borrower of the Obligations on the terms set forth in the Guaranty.

NOW, THEREFORE, for value received and in consideration of the financial accommodations provided by Lender to Borrower under the Loan Agreement and other transactions contemplated thereby, Guarantors unconditionally guarantee (i) the full and prompt payment and performance when due, whether at maturity or earlier, by reason of acceleration or otherwise, and at all times thereafter, of all liabilities of Borrower to Lender and (ii) the prompt, full and faithful discharge by Borrower of each and every term, condition, agreement, representation and warranty now or hereafter made by Borrower to Lender under the Loan Agreement or any document or instrument delivered by Borrower to the Purchasers in connection therewith or pursuant thereto (which, together with the liabilities described in clause (i) hereof, are collectively referred to herein as the "Borrower's Liabilities"). The Guarantors further agree to pay all reasonable out-of-pocket costs and expenses, including, without limitation, all court costs and reasonable attorneys' and paralegals' fees paid or incurred by Lender, in endeavoring to collect all or any part of Borrower's Liabilities from, or in prosecuting any action against the Guarantors of all or any part of Borrower's Liabilities. All amounts payable by the Guarantors under this Guaranty shall be payable pursuant to the terms of the Loan Agreement upon demand by Lender.

Notwithstanding any provision of this Guaranty to the contrary, it is intended that this Guaranty, and any liens and security interests granted by the Guarantors to secure this Guaranty, not constitute a Fraudulent Conveyance (as defined below). Consequently, the Guarantors agree that if this Guaranty, or any liens or security interests securing this Guaranty, would, but for the application of this sentence, constitute a Fraudulent Conveyance, this Guaranty and each such lien and security interest shall be valid and enforceable only to the maximum extent that would not cause this Guaranty or such lien or security interest to constitute a Fraudulent Conveyance, and this Guaranty shall automatically be deemed to have been amended accordingly at all relevant times. For purposes hereof, "Fraudulent Conveyance" means a fraudulent conveyance under Section 548 of the

"Bankruptcy Code" (as hereinafter defined) or a fraudulent conveyance or fraudulent transfer under the provisions of any applicable fraudulent conveyance or fraudulent transfer law or similar law of any state, nation or other governmental unit, as in effect from time to time.

The Guarantors hereby agree that, except as hereinafter provided, and to the extent permitted by applicable law, its obligations under this Guaranty shall be unconditional, irrespective of (i) the validity or enforceability of Borrower's Liabilities or any part thereof, or of any promissory note or other document evidencing all or any part of Borrower's Liabilities, (ii) the absence of any attempt to collect Borrower's Liabilities from Borrower or any other Guarantors or other action to enforce the same, (iii) the waiver or consent by any Lender with respect to any provision of any instrument evidencing Borrower's Liabilities, or any part thereof, or any other agreement heretofore, now or hereafter executed by Borrower and delivered to Lender, (iv) failure by any Lender to take any steps to perfect and maintain its security interest in, or to preserve its rights to, any security or collateral for Borrower's Liabilities, (v) the institution of any proceeding under Chapter 11 of Title 11 of the United States Code (11 U.S.C. Section 101 et seq.), as amended (the "Bankruptcy Code"), or any similar proceeding, by or against Borrower, or any Lender's election in any such proceeding of the application of Section 1111(b)(2) of the Bankruptcy Code, (vi) any borrowing or grant of a security interest by Borrower as debtor-in-possession, under Section 364 of the Bankruptcy Code, (vii) the disallowance, under Section 502 of the Bankruptcy Code, of all or any portion of Lender's claim(s) for repayment of Borrower's Liabilities, or (viii) any other circumstance which might otherwise constitute a legal or equitable discharge or defense of the Guarantors.

The Guarantors hereby waive diligence, presentment, demand of payment, filing of claims with a court in the event of receivership or bankruptcy of Borrower, protest or notice with respect to Borrower's Liabilities and all demands whatsoever, and covenants that this Guaranty will not be discharged, except by complete performance of the obligations and liabilities contained herein. Upon the occurrence and during the continuance of an Event of Default under the Loan Agreement, Lender may, at its sole election, proceed directly and at once, without notice, against the Guarantors to collect and recover the full amount or any portion of Borrower's Liabilities, without first proceeding against any other person, firm, or corporation, or against any security or collateral for Borrower's Liabilities.

Lender is hereby authorized, without notice or demand and without affecting the liability of the Guarantors hereunder, at any time and from time to time to (i) renew, extend, accelerate or otherwise change the time for payment of, or other terms relating to Borrower's Liabilities or otherwise modify, amend or change the terms of any debenture, note or other agreement, document or instrument now or hereafter executed by Borrower and delivered to Lender; (ii) accept partial payments on Borrower's Liabilities; (iii) take and hold security or collateral for the payment of Borrower's Liabilities guaranteed hereby, or for the payment of this Guaranty, or for the payment of any other guaranties of Borrower's Liabilities or other liabilities of Borrower, and exchange, enforce, waive and release any such security or collateral; (iv) apply such security or collateral and direct the order or manner of sale thereof as in their sole discretion they may determine; and (v) settle, release, compromise, collect or otherwise liquidate Borrower's Liabilities and any security or collateral therefor in any manner, without affecting or impairing the obligations of the Guarantors hereunder. Lender shall have the exclusive right to determine the time and manner of application of any payments or credits, whether received from the Borrower or any other source, and such determination shall be binding on the Guarantor. All such payments and credits may be applied, reversed and reapplied, in whole or in part, to any of Borrower's Liabilities as Lender shall determine

in their sole discretion without affecting the validity or enforceability of this Guaranty (unless otherwise required pursuant to the Loan Agreement).

The Guarantors hereby confirm and reaffirm the granting by the Guarantors to Lender, of a perfected lien on and security interest in all of the Collateral described in Section II of the Watson Guarantors Security Agreement dated as of the date hereof between the Guarantors and the Lender as collateral security for all liabilities of the Guarantors, including without limitation all liabilities, obligations and indebtedness owing by the Guarantors to Lender arising under or relating to this Guaranty. In addition, at any time after maturity of Borrower's Liabilities by reason of acceleration or otherwise, any Lender may, in its sole discretion, without notice to the Guarantors and regardless of the acceptance of any security or collateral for the payment hereof, appropriate and apply toward the payment of Borrower's Liabilities (i) any indebtedness due or to become due from such Lender to the Guarantors, and (ii) any moneys, credits or other property belonging to the Guarantors, at any time held by or coming into the possession of such Lender whether for deposit or otherwise.

The Guarantors hereby assume responsibility for keeping themselves informed of the financial condition of Borrower, and any and all endorsers and/or other guarantors of any instrument or document evidencing all or any part of Borrower's Liabilities and of all other circumstances bearing upon the risk of nonpayment of Borrower's Liabilities or any part thereof that diligent inquiry would reveal and the Guarantors hereby agree that Lender shall not have any duty to advise the Guarantors of information known to any of them regarding such condition or any such circumstances or to undertake any investigation not a part of their respective regular business routines. If any Lender, in its sole discretion, undertakes at any time or from time to time to provide any such information to any the Guarantors, such Lender shall not be under any obligation to update any such information or to provide any such information to the Guarantors on any subsequent occasion.

The Guarantors consent and agree that Lender shall not be under any obligation to marshal any assets in favor of the Guarantors or against or in payment of any or all of Borrower's Liabilities. The Guarantors further agree that, to the extent that Borrower makes a payment or payments to Lender or Lender receive any proceeds of collateral, which payment or payments or any part thereof are subsequently invalidated, declared to be fraudulent or preferential, set aside and/or required to be repaid to Borrower, its estate, trustee, receiver or any other party, including, without limitation, the Guarantors, under any bankruptcy law or state or federal statutory or common law, then to the extent of such payment or repayment, Borrower's Liabilities or the part thereof which has been paid, reduced or satisfied by such amount, and the Guarantors' obligations hereunder with respect to such portion of Borrower's Liabilities, shall be reinstated and continued in full force and effect as of the date such initial payment, reduction or satisfaction occurred.

Until payment in full of all of Borrower's Liabilities, the Guarantors hereby waive any and all claims (including without limitation any claim for reimbursement, contribution or subrogation) of the Guarantors against Borrower, any endorser or any other Guarantors of all or any part of Borrower's Liabilities, or against any of Borrower's properties, arising by reason of any payment by the Guarantors to Lender pursuant to the provisions hereof.

Each Lender may, to the extent and in the manner set forth in the Loan Agreement, sell or assign Borrower's Liabilities or any part thereof, or grant participations therein, and in any such event each and every permitted assignee or holder of, or participant in, all or any of Borrower's Liabilities shall have the right to enforce this Guaranty, by suit or otherwise for the benefit of such assignee, holder, or participant, as fully as if herein by name specifically given such right.

The Guarantors hereby represent and warrant that: (a) each of them is a corporation duly organized, validly existing and in good standing under the laws of the state of incorporation; (b) each of them is duly authorized and empowered to execute and deliver the Guaranty; (c) all corporate action on the part of the Guarantors requisite for the due execution and delivery of the Guaranty and the due granting and creation of the security interests referred to herein has been duly and effectively taken and (d) the Guarantors' chief executive offices are located at Halsey Drug Co., Inc., 695 No. Perryville Road, Rockford, Illinois, 61107 and 16235 State Road 17, Culver, Indiana, respectively.

This Guaranty shall be binding upon the Guarantors and upon the successors (including without limitation, any receiver, trustee or debtor in possession of or for the Guarantors) of the Guarantors and shall inure to the benefit of Lender and their respective successors and permitted assigns.

This Guaranty shall continue in full force and effect, and Lender shall be entitled to make loans and advances and extend financial accommodations to Borrower on the faith hereof, until such time as all of Borrower's Liabilities have been paid in full and discharged and the Loan Agreement has been terminated.

Wherever possible each provision of this Guaranty shall be interpreted in such manner as to be effective and valid under applicable law, but if any provision of this Guaranty shall be prohibited by or invalid under such law, such provision shall be ineffective to the extent of such prohibition or invalidity without invalidating the remainder of such provision or the remaining provisions of this Guaranty.

THIS GUARANTY SHALL BE GOVERNED AND CONTROLLED BY THE LAWS OF THE STATE OF CALIFORNIA.

The Guarantors irrevocably agree that, subject to the sole and absolute election of Lender, ALL ACTIONS OR PROCEEDINGS IN ANY WAY, MANNER OR RESPECT, ARISING OUT OF OR FROM OR RELATED TO THIS GUARANTY SHALL BE LITIGATED IN COURTS HAVING SITUS WITHIN THE STATE OF CALIFORNIA.

THE GUARANTORS HEREBY CONSENT AND SUBMIT TO THE JURISDICTION OF ANY LOCAL, STATE OR FEDERAL COURTS LOCATED WITHIN ORANGE COUNTY, CALIFORNIA and waives the defense of "forum non conveniens." The Guarantors waive personal service of any and all process, and consents that all such service of process may be made by certified mail, return receipt requested, directed to the Guarantors at the address indicated in the Agent's records; and service so made shall be complete five (5) days after the same has been deposited in the U.S. mails as aforesaid. THE GUARANTORS HEREBY WAIVE ANY RIGHT IT MAY HAVE TO TRANSFER OR CHANGE THE VENUE OF ANY LITIGATION BROUGHT AGAINST THE GUARANTORS BY LENDER IN ACCORDANCE WITH THIS PARAGRAPH.

THE GUARANTORS HEREBY WAIVE ALL RIGHTS TO TRIAL BY JURY IN ANY ACTION OR PROCEEDING WHICH PERTAINS DIRECTLY OR INDIRECTLY TO THIS GUARANTY.

IN WITNESS WHEREOF, this Guaranty has been duly executed by the undersigned as of this 29th day as of March, 2000.

HALSEY PHARMACEUTICAL, INC.,
a Delaware corporation

/s/ Michael Reicher
Name:
Title: Chief Executive Officer

HOUBA, INC.,
an Indiana corporation

/s/ Michael Reicher
Name:
Title: Chief Executive Officer

WATSON GUARANTORS SECURITY AGREEMENT

THIS WATSON GUARANTORS SECURITY AGREEMENT ("Security Agreement") is made and entered into as of March 29, 2000, by HALSEY PHARMACEUTICALS, INC., a Delaware corporation ("HP, Inc.," and a "Guarantor") and HOUBA, INC., an Indiana corporation (individually, a "Guarantor," and together with HP, Inc., the "Guarantors"); and WATSON PHARMACEUTICALS, INC., a Nevada corporation ("Lender").

W I T N E S S E T H

WHEREAS, Halsey Drug Co., Inc., a New York corporation (the "Borrower") and Lender have entered into a Loan Agreement dated as of the date hereof (as the same may be amended, modified, supplemented or restated from time to time, the "Loan Agreement"; terms which are capitalized herein and not otherwise defined shall have the meanings ascribed to them in the Loan Agreement);

WHEREAS, Each of the Guarantors has executed and delivered to Lender the Watson Guaranty dated the date hereof (the "Watson Guaranty") of Borrower's Obligations; and

WHEREAS, Lender requires, as a condition precedent to the effectiveness of the Loan Agreement, that the Guarantors (i) grant to Lender a security interest in and to the Collateral (as defined in Section II below) and (ii) execute and deliver this Security Agreement in order to secure the payment and performance by such Guarantor of the Guaranty.

NOW, THEREFORE, in consideration of the premises and in order to induce Lender to enter into and perform the Loan Agreement, each Guarantor hereby agrees as follows:

SECTION I

CREATION OF SECURITY INTEREST

Each Guarantor hereby pledges, assigns and grants to Lender a continuing perfected lien on and security interest in all of such Guarantor's right, title and interest in and to the Collateral (as defined in Section II below) in order to secure the payment and performance of all Obligations owing by such Guarantor.

SECTION II

COLLATERAL

For purposes of this Security Agreement, the term "Collateral" shall mean, with respect to each Guarantor, all of the kinds and types of real and personal property described in subsections A through F hereof, whether now owned or hereafter at any time arising, acquired or created by such Guarantor and wherever located, and includes all replacements, additions, accessions, substitutions, repairs, proceeds and products relating thereto or therefrom, and all documents, ledger sheets and files of such Guarantor relating thereto. "Proceeds" hereunder include (i) whatever is now or hereafter received by such Guarantor upon the sale, exchange, collection or other disposition of any item of Collateral, whether such proceeds constitute inventory, accounts, accounts receivable, general intangibles, instruments, securities (including, without limitation, United States of America Treasury

Bills), credits, claims, demands, documents, letters of credit and letter of credit proceeds, chattel paper, documents of title, certificates of title, certificates of deposit, warehouse receipts, bills of lading, leases, deposit accounts, money, tax refund claims, contract rights, goods or equipment and (ii) any such items which are now or hereafter acquired by such Guarantor with any proceeds of Collateral hereunder:

A. Accounts. All of such Guarantor's accounts, whether now existing or existing in the future, including without limitation (i) all accounts receivable (whether or not specifically listed on schedules furnished to Lender), including, without limitation, all accounts created by or arising from all of such Guarantor's sales of goods or rendition of services made under any of such Guarantor's trade names, or through any of its divisions, (ii) all unpaid seller's rights (including rescission, replevin, reclamation and stoppage in transit) relating to the foregoing or arising therefrom, (iii) all rights to any goods represented by any of the foregoing, including returned or repossessed goods, (iv) all reserves and credit balances held by such Guarantor with respect to any such accounts receivable or account debtors and (v) all guarantees or collateral for any of the foregoing (all of the foregoing property and similar property being hereinafter referred to as "Accounts");

B. Inventory. All of such Guarantor's inventory, including without limitation (i) all raw materials, work in process, parts, components, assemblies, supplies and materials used or consumed in such Guarantor's businesses, wherever located and whether in the possession of such Guarantor or any other Person (for the purposes of this Company Security Agreement, the term "Person" means any individual, sole proprietorship, partnership, joint venture, trust, unincorporated organization, association, corporation, institution, entity, party or government, including any division, agency or department thereof); (ii) all goods, wares and merchandise, finished or unfinished, held for sale or lease or leased or furnished or to be furnished under contracts of service, wherever located and whether in the possession of such Guarantor or any other person or entity; and (iii) all goods returned to or repossessed by such Guarantor (all of the foregoing property being hereinafter referred to as "Inventory");

C. Equipment. All of the equipment owned or leased by such Guarantor, including, without limitation, machinery, equipment, office equipment and supplies, computers and related equipment, furniture, furnishings, tools, tooling, jigs, dies, fixtures, manufacturing implements, fork lifts, trucks, trailers, motor vehicles, and other equipment (all of the foregoing property being hereinafter referred to as "Equipment");

D. Intangibles. All of such Guarantor's general intangibles, instruments, securities (including without limitation United States of America Treasury Bills), credits, claims, demands, documents, letters of credit and letter of credit proceeds, chattel paper, documents of title, certificates of title, certificates of deposit, warehouse receipts, bills of lading, leases which are permitted to be assigned or pledged, deposit accounts, money, tax refund claims, contract rights which are permitted to be assigned or pledged (all of the foregoing property being hereinafter referred to as "Intangibles"); and

E. Intellectual Property. All of each Guarantor's intellectual property, including, without limitation, New Drug Applications, Investigatory New Drug Applications, Abbreviated New Drug Applications, Alternative New Drug Applications, registrations and quotas as issued by the Drug Enforcement Administration and/or the Attorney General of the United States pursuant to the Controlled Substances Act, certifications, permits and approvals of federal and state governmental agencies, patents, patent applications, trademarks, trademark applications, service marks, service

mark applications, trade names, technical knowledge and processes, formal or informal licensing arrangements which are permitted to be assigned or pledged, blueprints, technical specifications, computer software, copyrights, copyright applications and other trade secrets, and all embodiments thereof, and rights thereto, including, without limitation, all of such Guarantor's rights to use the patents, trademarks, copyrights, service marks, or other property of the aforesaid nature of other Persons now or hereafter licensed to such Guarantor, together with the goodwill of the business symbolized by or connected with such Guarantor's trademarks, copyrights, service marks, licenses and the other rights included in this section II(E).

F. Real Property. All right, title and interest of the Guarantors in any real property, including without limitation that certain real property located in Culver, Indiana, commonly known as 16235 State Road 17, Culver, Indiana.

SECTION III

THE GUARANTORS' REPRESENTATIONS AND WARRANTIES

Each Guarantor severally represents and warrants as follows:

A. Places of Business. Such Guarantor has no places of business, or warehouses in which it leases space, other than those set forth on Section III A. of Schedule A, a copy of which is attached hereto and made a part hereof ("Schedule A").

B. Location of Collateral. Except for the movement of Collateral from time to time from one place of business or warehouse listed on Section III A. of Schedule A to another place of business or warehouse listed on Section III A. of such Schedule A, the Collateral is located at such Guarantor's chief executive offices or other places of business or warehouses listed on such Section III A. of Schedule A, and not at any other location.

C. Restrictions on Collateral Disposition. Except as otherwise provided in the Loan Agreement, none of the Collateral is subject to contractual obligations that may restrict or inhibit Lender's rights or ability to sell or dispose of the Collateral or any part thereof after the occurrence of an Event of Default.

D. Status of Accounts. Each Account is based on an actual and bona fide rendition of services to customers, made by such Guarantor in the ordinary course of its business; the Accounts created are its exclusive property and are not and shall not be subject to any lien, consignment arrangement, encumbrance, security interest or financing statement whatsoever, except as otherwise provided in Section III D. of Schedule A, and to the best knowledge of such Guarantor, such Guarantor's customers have accepted the services, and owe and are obligated to pay the full amounts stated in the invoices according to their terms, without any dispute, offset, defense or counterclaim.

SECTION IV

COVENANTS OF THE GUARANTORS

Each Guarantor agrees (which agreements shall be several as to each Guarantor except as otherwise provided) as follows:

A. **Defend Against Claims.** Such Guarantor will defend the Collateral against all claims and demands of all persons at any time claiming the same or any interest therein unless both Lender and such Guarantor determine that the claim or demand is not material and that, consequently, such defense would not be consistent with good business judgment. Such Guarantor will permit any lien notices with respect to the Collateral or any portion thereof to exist or be on file in any public office except for those in favor of Lender and those permitted under the terms of the Loan Agreement.

B. **Change in Collateral Location.** Such Guarantor will not (i) change its corporate name, (ii) change the location of its chief executive office or establish any place of business other than those specified in Section III A. of Schedule A, or (iii) move or permit movement of the Collateral from the locations specified thereon except from one such location to another such location, unless in each case such Guarantor shall have given Lender at least thirty (30) days prior written notice thereof, and shall have, in advance, executed and caused to be filed and/or delivered to Lender any financing statements or other documents required by Lender to perfect the security interest of Lender in the Collateral in accordance with Section IV C. hereof, all in form and substance satisfactory to Lender.

C. **Additional Financing Statements.** Promptly upon the reasonable request of Lender, such Guarantor will execute and deliver or use its reasonable efforts to procure any document, give any notices, execute and file any financing statements, mortgages or other documents, all in form and substance satisfactory to Lender, mark any chattel paper, deliver any chattel paper or instruments to Lender and take any other actions that are necessary or, in the opinion of Lender, desirable to perfect or continue the perfection and the first priority of Lender's security interest in the Collateral, to protect the Collateral against the rights, claims, or interests of third persons, or to effect the purposes of this Security Agreement. Such Guarantor will pay the costs incurred in connection with any of the foregoing.

D. **Additional Liens; Transfers.** Without the prior written consent of Lender, such Guarantor will not, in any way, hypothecate or create or permit to exist any lien, security interest, charge or encumbrance on or other interest in the Collateral, other than those permitted under the terms of the Loan Agreement, and such Guarantor will not sell, transfer, assign, pledge, collaterally assign, exchange or otherwise dispose of the Collateral, other than the sale of Inventory in the ordinary course of business and the sale of obsolete or worn out Equipment. Notwithstanding the foregoing, if the proceeds of any such sale consist of notes, instruments, documents of title, letters of credit or chattel paper, such proceeds shall be promptly delivered to Lender to be held as Collateral hereunder. If the Collateral, or any part thereof, is sold, transferred, assigned, exchanged, or otherwise disposed of in violation of these provisions, the security interest of Lender shall continue in such Collateral or part thereof notwithstanding such sale, transfer, assignment, exchange or other disposition, and such Guarantor will hold the proceeds thereof for the benefit of Lender, and promptly transfer such proceeds to Lender in kind.

E. **Contractual Obligations.** Such Guarantor will not enter into any contractual obligations which may restrict or inhibit Lender's rights or ability to sell or otherwise dispose of the Collateral or any part thereof after the occurrence or during the continuance of an Event of Default.

F. **Lender's Right to Protect Collateral.** Upon the occurrence or continuance of an Event of Default, Lender shall have the right at any time to make any payments and do any other acts Lender may deem necessary to protect the security interests of Lender in the Collateral, including, without limitation, the rights to pay, purchase, contest or compromise any encumbrance, charge or

lien which, in the reasonable judgment of Lender, appears to be prior to or superior to the security interests granted hereunder, and appear in and defend any action or proceeding purporting to affect its security interests in, and/or the value of, the Collateral. The Guarantors hereby jointly and severally agree to reimburse Lender for all payments made and expenses incurred under this Security Agreement including reasonable fees, expenses and disbursements of attorneys and paralegals acting for Lender, including any of the foregoing payments under, or acts taken to protect its security interests in, the Collateral, which amounts shall be secured under this Security Agreement, and agree they shall be bound by any payment made or act taken by Lender hereunder absent Lender's gross negligence or willful misconduct. Lender shall have no obligation to make any of the foregoing payments or perform any of the foregoing acts.

G. Further Obligations With Respect to Accounts. In furtherance of the continuing assignment and security interest in the Accounts of such Guarantor granted pursuant to this Security Agreement, upon the creation of Accounts, upon Lender's request, such Guarantor will execute and deliver to Lender in such form and manner as Lender may require, solely for its convenience in maintaining records of Collateral, such confirmatory schedules of Accounts, and other appropriate reports designating, identifying and describing the Accounts as Lender may reasonably require. In addition, upon Lender's request, such Guarantor shall provide Lender with copies of agreements with, or purchase orders from, the customers of such Guarantor and copies of invoices to customers, proof of shipment or delivery and such other documentation and information relating to said Accounts and other Collateral as Lender may reasonably require. Furthermore, upon Lender's request, such Guarantor shall deliver to Lender any documents or certificates of title issued with respect to any property included in the Collateral, and any promissory notes, letters of credit or instruments related to or otherwise in connection with any property included in the Collateral, which in any such case came into the possession of such Guarantor, or shall cause the issuer thereof to deliver any of the same directly to Lender, in each case with any necessary endorsements in favor of Lender. Failure to provide Lender with any of the foregoing shall in no way affect, diminish, modify or otherwise limit the security interests granted herein. Each Guarantor hereby authorizes Lender to regard such Guarantor's printed name or rubber stamp signature on assignment schedules or invoices as the equivalent of a manual signature by such Guarantor's authorized officers or agents.

H. Insurance. Such Guarantor agrees to maintain public liability insurance, third party property damage insurance and replacement value insurance on the Collateral under such policies of insurance, with such insurance companies, in such amounts and covering such risks as are at all times satisfactory to Lender in its commercially reasonable judgment. All policies covering the Collateral are to name Lender as an additional insured and the loss payee in case of loss, and are to contain such other provisions as Lender may reasonably require to fully protect Lender's interest in the Collateral and to any payments to be made under such policies.

I. Taxes. Such Guarantor agrees to pay, when due, all taxes lawfully levied or assessed against such Guarantor or any of the Collateral before any penalty or interest accrues thereon; provided, however, that, unless such taxes have become a Federal tax or Employment Retirement Security Income Act lien on any of the assets of such Guarantor, no such tax need be paid if the same is being contested, in good faith, by appropriate proceedings promptly instituted and diligently conducted and if an adequate reserve or other appropriate provision shall have been made therefor as required in order to be in conformity with generally accepted accounting principles and procedures in effect in the United States of America.

J. Compliance with Laws. Such Guarantor agrees to comply in all material respects with all requirements of law applicable to the Collateral or any part thereof, or to the operation of its business or its assets generally, unless such Guarantor contests any such requirements of law in a reasonable manner and in good faith. Such Guarantor agrees to maintain in full force and effect, its respective licenses and permits granted by any governmental authority as may be necessary or advisable for such Guarantor to conduct its business in all material respects.

K. Maintenance of Property. Such Guarantor agrees to keep all property useful and necessary to its business in good working order and condition (ordinary wear and tear excepted) and not to commit or suffer any waste with respect to any of their properties.

L. Environmental and Other Matters. Such Guarantor will conduct its business so as to comply in all material respects with all environmental, land use, occupational, safety or health laws, regulations, directions, ordinances, criteria and guidelines in all jurisdictions in which it is or may at any time be doing business, except to the extent that such Guarantor is contesting, in good faith by appropriate legal, administrative or other proceedings, any such law, regulation, direction, ordinance, criteria, guideline, or interpretation thereof or application thereof; provided, further, that such Guarantor shall comply with the order of any court or other governmental authority relating to such laws unless such Guarantor shall currently be prosecuting an appeal, proceedings for review or administrative proceedings and shall have secured a stay of enforcement or execution or other arrangement postponing enforcement or execution pending such appeal, proceedings for review or administrative proceedings.

M. Further Assurances. Such Guarantor shall take all such further actions and execute all such further documents and instruments (including, but not limited to, collateral assignments of Intellectual Property and Intangibles or any portion thereof) as Lender may at any time reasonably determine in its sole discretion to be necessary or desirable to further carry out and consummate the transactions contemplated by the Loan Agreement and the documentation relating thereto, including this Security Agreement, and to perfect or protect the liens (and the priority status thereof) of Lender in the Collateral.

SECTION V

REMEDIES

A. Obtaining the Collateral Upon Default. If any Event of Default shall have occurred and be continuing, then and in every such case, subject to any mandatory requirements of applicable law then in effect, Lender, in addition to any rights now or hereafter existing under applicable law, shall have all rights as a secured creditor under the Uniform Commercial Code in all relevant jurisdictions and may:

(a) personally, or by agents or attorneys, immediately retake possession of the Collateral or any part thereof, from any Guarantor or any other Person who then has possession of any part thereof, with or without notice or process of law, and for that purpose may enter upon such Guarantor's premises where any of the Collateral is located and remove the same and use in connection with such removal any and all services, supplies, aids and other facilities of such Guarantor;

(b) instruct the obligor or obligors on any agreement, instrument or other obligation (including, without limitation, the Accounts) constituting the Collateral to make any payment required by the terms of such instrument or agreement directly to Lender;

(c) withdraw all monies, securities and instruments held pursuant to any pledge arrangement for application to the Obligations;

(d) sell, assign or otherwise liquidate, or direct any Guarantor to sell, assign or otherwise liquidate, any or all of the Collateral or any part thereof, and take possession of the proceeds of any such sale or liquidation;

(e) take possession of the Collateral or any part thereof, by directing any Guarantor in writing to deliver the same to Lender at any place or places designated by Lender, in which event such Guarantor shall at its own expense:

(i) forthwith cause the same to be moved to the place or places so designated by Lender and there delivered to Lender,

(ii) store and keep any Collateral so delivered to Lender at such place or places pending further action by Lender as provided in Section V B., and

(iii) while the Collateral shall be so stored and kept, provide such guards and maintenance services as shall be necessary to protect the same and to preserve and maintain the Collateral in good condition; it being understood that any Guarantor's obligation to so deliver the Collateral is of the essence of this Security Agreement and that, accordingly, upon application to a court of equity having jurisdiction, Lender shall be entitled to a decree requiring specific performance by such Guarantor of said obligation.

B. Disposition of the Collateral. Any collateral repossessed by Lender under or pursuant to Section V A. and any other Collateral whether or not so repossessed by Lender, may be sold, assigned, leased or otherwise disposed of under one or more contracts or as an entirety, and without the necessity of gathering at the place of sale the property to be sold, and in general in such manner, at such time or times, at such place or places and on such terms as Lender may, in compliance with any mandatory requirements of applicable law, determine to be commercially reasonable. Any of the Collateral may be sold, leased or otherwise disposed of, in the condition in which the same existed when taken by Lender or after any overhaul or repair which Lender shall determine to be commercially reasonable. Any such disposition which shall be a private sale or other private proceedings permitted by such requirements shall be made upon not less than ten (10) days' written notice to such Guarantor specifying the time at which such disposition is to be made and the intended sale price or other consideration therefor, and shall be subject, for the ten (10) days after the giving of such notice, to the right of such Guarantor or any nominee of such Guarantor to acquire the Collateral involved at a price or for such other consideration at least equal to the intended sale price or other consideration so specified. Any such disposition which shall be a public sale permitted by such requirements shall be made upon not less than ten (10) days' written notice to such Guarantor specifying the time and place of such sale and, in the absence of applicable requirements of law, shall be by public auction (which may, at the option of Lender, be subject to reserve), after publication of notice of such auction not less than ten (10) days prior thereto in two (2) newspapers in general circulation in the City of New York, as Lender may determine. To the extent permitted by any such

requirement of law, Lender may bid for and become the purchaser of the Collateral or any item thereof, offered for sale in accordance with this Section without accountability to such Guarantor (except to the extent of surplus money received). If, under mandatory requirements of applicable law, Lender shall be required to make disposition of the Collateral within a period of time which does not permit the giving of notice to such Guarantor as hereinabove specified, Lender need give such Guarantor only such notice of disposition as shall be reasonably practicable in view of such mandatory requirements of applicable law.

C. Power of Attorney. Each Guarantor hereby irrevocably authorizes and appoints Lender, or any Person that Lender may designate, as such Guarantor's attorney-in-fact, at such Guarantor's cost and expense, to exercise all of the following powers upon and at any time after the occurrence and during the continuance of an Event of Default, which powers, being coupled with an interest, shall be irrevocable until all of the Obligations owing by such Guarantor shall have been paid and satisfied in full:

(a) accelerate or extend the time of payment, compromise, issue credits, bring suit or administer and otherwise collect Accounts or proceeds of any Collateral;

(b) receive, open and dispose of all mail addressed to such Guarantor and notify postal authorities to change the address for delivery thereof to such address as Lender may designate;

(c) give customers indebted on Accounts notice of Lender's interest therein, and/or to instruct such customers to make payment directly to Lender for such Guarantor's account;

(d) convey any item of Collateral to any purchaser thereof;

(e) give any notices or record any liens under Section IV C. hereof; and

(f) make any payments or take any acts under Section IV F. hereof.

Lender's authority under this Section V C. shall include, without limitation, the authority to execute and give receipt for any certificate of ownership or any document, transfer title to any item of Collateral, sign such Guarantor's name on all financing statements or any other documents deemed necessary or appropriate to preserve, protect or perfect the security interest in the Collateral and to file the same, prepare, file and sign such Guarantor's name on any notice of lien, assignment or satisfaction of lien or similar document in connection with any Account and prepare, file and sign such Guarantor's name on a proof of claim in bankruptcy or similar document against any customer of such Guarantor, and to take any other actions arising from or incident to the rights, powers and remedies granted to Lender in this Security Agreement. This power of attorney is coupled with an interest and is irrevocable by such Guarantor.

D. Waiver of Claims. Except as otherwise provided in this Security Agreement, EACH GUARANTOR HEREBY WAIVES, TO THE EXTENT PERMITTED BY APPLICABLE LAW, NOTICE AND JUDICIAL HEARING IN CONNECTION WITH LENDER'S TAKING POSSESSION OF OR DISPOSING OF ANY OF THE COLLATERAL, INCLUDING, WITHOUT LIMITATION, ANY AND ALL PRIOR NOTICE AND HEARING FOR ANY PREJUDGMENT REMEDY OR REMEDIES AND ANY SUCH RIGHT WHICH ANY GUARANTOR WOULD OTHERWISE HAVE UNDER THE CONSTITUTION OR ANY STATUTE OF THE UNITED

STATES OR OF ANY STATE, and each Guarantor hereby further waives, to the extent permitted by law:

(a) all damages occasioned by such taking of possession except any damages which are the direct result of Lender's gross negligence or willful misconduct;

(b) all other requirements as to the time, place and terms of sale or other requirements with respect to the enforcement of Lender's rights hereunder, except as expressly provided herein; and

(c) all rights of redemption, appraisalment, valuation, stay, extension or moratorium now or hereafter in force under any applicable law in order to prevent or delay the enforcement of this Security Agreement or the absolute sale of the Collateral or any portion thereof, and such Guarantor, for itself and all who may claim under it, insofar as it or they now or hereafter lawfully may, hereby waives the benefit of all such laws.

Any sale of, or the grant of options to purchase, or any other realization upon any Collateral shall operate to divest all right, title, interest, claim and demand, either at law or in equity, of such Guarantor therein and thereto, and shall be a perpetual bar both at law and in equity against such Guarantor and against any and all persons claiming or attempting to claim the Collateral so sold, optioned or realized upon, or any part thereof, from, through and under such Guarantor.

E. Remedies Cumulative. Each and every right, power and remedy hereby specifically given to Lender shall be in addition to every other right, power and remedy specifically given under this Security Agreement, under the Loan Agreement or under other documentation relating thereto or now or hereafter existing at law or in equity, or by statute, and each and every right, power and remedy whether specifically herein given or otherwise existing may be exercised from time to time or simultaneously and as often and in such order as may be deemed expedient by Lender. All such rights, powers and remedies shall be cumulative and the exercise or the beginning of exercise of one shall not be deemed a waiver of the right to exercise of any other or others. No delay or omission of Lender in the exercise of any such right, power or remedy and no renewal or extension of any of the Obligations shall impair any such right, power or remedy or shall be construed to be a waiver of any Default or Event of Default or any acquiescence therein.

SECTION VI

MISCELLANEOUS PROVISIONS

A. Notices. All notices, approvals, consents or other communications required or desired to be given hereunder shall be delivered in person, by facsimile transmission followed promptly by first class mail or by overnight mail, and delivered if to any Guarantor, then to the attention of Mr. Michael Reicher, c/o Halsey Drug. Co., Inc., 695 No. Perryville Road, Rockford, Illinois, 61107, fax no. (815) 399-9710, with a copy to John P. Reilly, Esq., c/o St. John & Wayne, L.L.P., 2 Penn Plaza East, Newark, New Jersey 07105, fax no. (973) 491-3407, and if to Lender, then to the attention of Chief Financial Officer, c/o Watson Pharmaceuticals, Inc., 311 Bonnie Circle, Corona, CA 92880, fax no. (909) 279-8094 (courtesy copy to Robert Funsten, Esq., General Counsel) with a copy to Lawrence B. Cohn, c/o Stradling Yocca, Carlson & Rauth, 660 Newport Center Drive, Suite 1600, Newport Beach, CA 92660, fax no. (212) 986-0604.

B. Headings. The headings in this Security Agreement are for purposes of reference only and shall not affect the meaning or construction of any provision of this Security Agreement.

C. Severability. The provisions of this Security Agreement are severable, and if any clause or provision shall be held invalid or unenforceable in whole or in part in any jurisdiction, then such invalidity or unenforceability shall affect, in that jurisdiction only, such clause or provision, or part thereof, and shall not in any manner affect such clause or provision in any other jurisdiction or any other clause or provision of this Security Agreement in any jurisdiction.

D. Amendments, Waivers and Consents. Any amendment or waiver of any provision of this Security Agreement and any consent to any departure by any Guarantor from any provision of this Security Agreement shall be effective only if made or given in writing signed by Lender.

E. Interpretation of Agreement. Time is of the essence in each provision of this Security Agreement of which time is an element. All terms not defined herein shall have the meaning set forth in the applicable Uniform Commercial Code. Acceptance of or acquiescence in a course of performance rendered under this Security Agreement shall not be relevant in determining the meaning of this Security Agreement even though the accepting or acquiescing party had knowledge of the nature of the performance and opportunity for objection.

F. Continuing Security Interest. This Company Security Agreement shall create a continuing security interest in the Collateral and shall (i) remain in full force and effect until indefeasible payment in full of the Obligations owing by the Guarantors, (ii) be binding upon each Guarantor, and its successors and assigns and (iii) inure to the benefit of Lender and its successors and assigns.

G. Reinstatement. To the extent permitted by law, this Security Agreement shall continue to be effective or be reinstated if at any time any amount received by Lender in respect of the Obligations owing by the Guarantors is rescinded or must otherwise be restored or returned by Lender upon the occurrence or during the pendency of any Event of Default, all as though such payments had not been made.

H. Survival of Provisions. All representations, warranties and covenants of the Guarantors contained herein shall survive the execution and delivery of this Security Agreement, and shall terminate only upon the full and final indefeasible payment and performance by the Guarantors of the Obligations secured hereby.

I. Setoff. Lender shall have all rights of setoff available at law or in equity.

J. Power of Attorney. In addition to the powers granted to Lender under Section V C., each Guarantor hereby irrevocably authorizes and appoints Lender, or any Person the Lender may designate, as such Guarantor's attorney-in-fact, at such Guarantor's cost and expense, to exercise all of the following powers, which being coupled with an interest, shall be irrevocable until all of the Obligations shall have been indefeasibly paid and satisfied in full:

(a) after the occurrence of an Event of Default, to receive, take, endorse, sign, assign and deliver, all in the name of Lender or such Guarantor, any and all checks, notes, drafts, and other documents or instruments relating to the Collateral; and

(b) to request, at any time from customers indebted on Accounts, verification of information concerning the Accounts and the amounts owing thereon.

K. Indemnification; Authority of Lender. Neither Lender nor any director, officer, employee, attorney or agent of Lender shall be liable to any Guarantor for any action taken or omitted to be taken by it or them hereunder, except for its or their own gross negligence or willful misconduct, nor shall Lender be responsible for the validity, effectiveness or sufficiency of this Security Agreement or of any document or security furnished pursuant hereto. Lender and its directors, officers, employees, attorneys and agents shall be entitled to rely on any communication, instrument or document reasonably believed by it or them to be genuine and correct and to have been signed or sent by the proper person or persons. Each Guarantor agrees to indemnify and hold harmless Lender and any other person from and against any and all costs, expenses (including reasonable fees, expenses and disbursements of attorneys and paralegals (including, without duplication, reasonable charges of inside counsel)), claims or liability incurred by Lender or such person hereunder, unless such claim or liability shall be due to willful misconduct or gross negligence on the part of Lender or such person.

L. Release; Termination of Agreement. Subject to the provisions of Section VI G. hereof, this Security Agreement shall terminate upon full and final indefeasible payment and performance of all the Obligations owing by each Guarantor. At such time, Lender shall, at the request of any Guarantor, reassign and redeliver to such Guarantor all of the Collateral hereunder which has not been sold, disposed of, retained or applied by Lender in accordance with the terms hereof. Such reassignment and redelivery shall be without warranty by or recourse to Lender, except as to the absence of any prior assignments by Lender of its interest in the Collateral, and shall be at the expense of such Guarantor.

M. Counterparts. This Security Agreement may be executed in one or more counterparts, each of which shall be deemed an original but all of which shall together constitute one and the same agreement.

N. GOVERNING LAW. THE VALIDITY, INTERPRETATION AND ENFORCEMENT OF THIS SECURITY AGREEMENT AND ANY DISPUTE ARISING OUT OF OR IN CONNECTION WITH THIS SECURITY AGREEMENT, WHETHER SOUNDING IN CONTRACT, TORT, EQUITY OR OTHERWISE, SHALL BE GOVERNED BY THE INTERNAL LAWS (AS OPPOSED TO THE CONFLICTS OF LAWS PROVISIONS) AND DECISIONS OF THE STATE OF CALIFORNIA.

O. SUBMISSION TO JURISDICTION. ALL DISPUTES BETWEEN ANY GUARANTOR AND LENDER, WHETHER SOUNDING IN CONTRACT, TORT, EQUITY OR OTHERWISE, SHALL BE RESOLVED ONLY BY STATE AND FEDERAL COURTS LOCATED IN ORANGE COUNTY, CALIFORNIA, AND THE COURTS TO WHICH AN APPEAL THEREFROM MAY BE TAKEN; PROVIDED, HOWEVER, THAT LENDER SHALL HAVE THE RIGHT, TO THE EXTENT PERMITTED BY APPLICABLE LAW, TO PROCEED AGAINST ANY GUARANTOR OR ITS PROPERTY IN ANY LOCATION REASONABLY SELECTED BY LENDER IN GOOD FAITH TO ENABLE LENDER TO REALIZE ON SUCH PROPERTY, OR TO ENFORCE A JUDGMENT OR OTHER COURT ORDER IN FAVOR OF LENDER. EACH GUARANTOR AGREES THAT IT WILL NOT ASSERT ANY PERMISSIVE COUNTERCLAIMS, SETOFFS OR CROSS-CLAIMS IN ANY PROCEEDING BROUGHT BY LENDER. EACH GUARANTOR WAIVES ANY OBJECTION THAT IT MAY HAVE TO THE

LOCATION OF THE COURT IN WHICH LENDER HAS COMMENCED A PROCEEDING, INCLUDING, WITHOUT LIMITATION, ANY OBJECTION TO THE LAYING OF VENUE OR BASED ON FORUM NON CONVENIENS.

P. SERVICE OF PROCESS. EACH GUARANTOR HEREBY IRREVOCABLY AGREES THAT SERVICE OF PROCESS IN ANY LEGAL ACTION OR PROCEEDING WITH RESPECT TO THIS SECURITY AGREEMENT MAY BE EFFECTED BY MAILING A COPY THEREOF BY REGISTERED OR CERTIFIED MAIL, POSTAGE PREPAID, TO SUCH GUARANTOR AT ITS ADDRESS SET FORTH IN SECTION VI A. HEREOF.

Q. JURY TRIAL. EACH GUARANTOR AND LENDER EACH HEREBY WAIVE ANY RIGHT TO A TRIAL BY JURY.

R. LIMITATION OF LIABILITY. LENDER SHALL NOT HAVE ANY LIABILITY TO ANY GUARANTOR (WHETHER SOUNDING IN TORT, CONTRACT, OR OTHERWISE) FOR LOSSES SUFFERED BY ANY GUARANTOR IN CONNECTION WITH, ARISING OUT OF, OR IN ANY WAY RELATED TO THE TRANSACTIONS OR RELATIONSHIPS CONTEMPLATED BY THIS SECURITY AGREEMENT, OR ANY ACT, OMISSION OR EVENT OCCURRING IN CONNECTION THEREWITH, UNLESS IT IS DETERMINED BY A FINAL AND NONAPPEALABLE JUDGMENT OR COURT ORDER BINDING ON LENDER, THAT THE LOSSES WERE THE RESULT OF ACTS OR OMISSIONS CONSTITUTING GROSS NEGLIGENCE OR WILLFUL MISCONDUCT.

S. Delays; Partial Exercise of Remedies. No delay or omission of Lender to exercise any right or remedy hereunder, whether before or after the happening of any Event of Default, shall impair any such right or shall operate as a waiver thereof or as a waiver of any such Event of Default. No single or partial exercise by Lender of any right or remedy shall preclude any other or further exercise thereof, or preclude any other right or remedy.

IN WITNESS WHEREOF, each Guarantor has caused this Security Agreement to be duly executed and delivered as of the day and year first above written.

HOUBA, INC.,
an Indiana corporation

By: /s/ Michael Reicher
Name:
Title: Chief Executive Officer

HALSEY PHARMACEUTICAL, INC.

By: /s/ Michael Reicher
Name:
Title: Chief Executive Officer

By its acceptance hereof, as of the day and year first above written, Lender agrees to be bound by the provisions hereof applicable to it.

WATSON PHARMACEUTICALS, INC.,
a Nevada corporation

By: /s/ Robert C. Funsten
Name:
Title: Senior Vice President

SCHEDULE A

III A. Locations of Collateral

1. Halsey Drug Co., Inc., 695 No. Perryville Road,
Rockford, Illinois, 61107
2. Halsey Pharmaceutical, Inc., 695 No. Perryville Road,
Rockford, Illinois, 61107
3. Houba, Inc. - 16235 State Road 17, Culver, IN

III D. Liens

1. All Guarantors: Schedule 8.3 to the Schedule of Exceptions
to the Loan Agreement is hereby incorporated by reference.
2. Houba, Inc.: Mortgage lien and security interest in favor of
the Existing Holders covering the real property in Culver,
Indiana.

SUBORDINATION AGREEMENT

Dated as of March 29, 2000

Among

WATSON PHARMACEUTICALS, INC.,

HALSEY DRUG CO., INC.,

The Existing Holders
(as defined herein)

and

THE GRANTORS AND GUARANTORS NAMED HEREIN

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SUBORDINATION AGREEMENT

This SUBORDINATION AGREEMENT (the "Agreement") is dated as of March 29, 2000 and is entered into by and among (i) WATSON PHARMACEUTICALS, INC., a Nevada corporation ("Watson"), (ii) HALSEY DRUG CO., INC., a New York corporation (the "Company"), (iii) the holders of the 5% Convertible Senior Secured Debentures issued by the Company pursuant to the Debenture and Warrant Purchase Agreement, dated March 10, 1998 (the "Galen Debenture Agreement"), by and among the Company, Galen Partners III, L.P. and the other signatories thereto, listed on Schedule 4 attached hereto (such holders, the "GALEN INVESTOR GROUP"), (iv) the holders of the 5% Convertible Senior Secured Debentures issued by the Company pursuant to the Debenture and Warrant Purchase Agreement, dated May 26, 1999 (the "Oracle Debenture Agreement"), by and among the Company, Oracle Strategic Partners, L.P. and the other signatories thereto, listed on Schedule 4 attached hereto (such holders, the "ORACLE INVESTOR GROUP"), and (v) the Grantors and Guarantors listed on the signature pages hereof. Certain capitalized terms used herein have the meanings ascribed thereto in Section 1.1.

RECITALS

A. Watson and the Company have entered into that certain Loan Agreement, dated as of March 29, 2000 (the "Loan Agreement"), pursuant to which Watson agreed to loan the Company the principal amount of Seventeen Million Five Hundred Thousand Dollars (\$17,500,000) (the "Loan").

B. The Company has issued its 5% Convertible Senior Secured Debentures Due March 15, 2003 to the Galen Investor Group pursuant to the Galen Debenture Agreement (such debentures, the "Galen Debentures") and to the Oracle Investor Group pursuant to the Oracle Debenture Agreement (such debentures, the "Oracle Debentures," and collectively with the Galen Debentures, the "Existing Debentures"). The holders of the Existing Debentures as of a given date are sometimes referred to herein as the "Existing Holders", and the Existing Holders and Watson are sometimes referred to herein collectively as the "Secured Creditors".

C. The Company and certain of its affiliates have entered into the Existing Security Documents and Existing Guaranty Agreements pursuant to which the Company and such affiliates secured the Company's obligations under the Existing Debentures and guaranteed the payment and performance of such obligations.

D. In connection with the execution of the Loan Agreement, the Company and Watson will be entering into new security documents (the "Watson Security Documents").

E. As an inducement to make the Loan, the Galen Investor Group and the Oracle Investor Group agree that (i) as among the Secured Creditors, Watson's security interest in the Collateral shall rank first in priority among the Secured Creditors; and (ii) proceeds received from enforcement of the Watson Security Documents and the Existing Security Documents will be applied first to the payment of the Company's obligations in respect of the Loan, and second, to the extent of any remaining proceeds, to the payment of the Company's obligations in respect of the Existing Debentures. The Company's and its affiliates' obligations under the Loan and the Existing Debentures are sometimes referred to collectively herein as the "Secured Obligations".

F. The parties hereto desire to set forth their agreement regarding the priority of Watson's security interest and the application to the Secured Obligations of cash received by the

Secured Creditors from dispositions of Collateral and the enforcement of the Existing Security Documents and the Watson Security Documents and the agreement of Watson, the Galen Investor Group and the Oracle Investor Group as to the decisions relating to the exercise of remedies under this Agreement and the Existing Security Documents and the Watson Security Documents.

G. It is a condition precedent to the effectiveness of the Loan Agreement that Watson, the Galen Investor Group, the Oracle Investor Group, the Company and its affiliates shall have entered into this Agreement.

In consideration of the above recitals and the mutual covenants contained herein, Watson, the Galen Investor Group, the Oracle Investor Group, the Company and the Grantors and Guarantors hereby agree as follows:

ARTICLE I

DEFINITIONS

SECTION 1.1. DEFINITIONS OF CERTAIN TERMS. As used herein, the following terms have the meanings set forth below:

"Agreement" is defined in the Preamble hereto.

"Business Day" shall mean any day other than a Saturday, Sunday or other day on which commercial banks are authorized or required to be closed in New York.

"Closing Date" means the date on which this Agreement becomes effective in accordance with Section 14.10.

"Collateral" means all the properties and assets of whatever nature, tangible or intangible, now owned or existing or hereafter acquired or arising, of any of the Grantors on or in which the Secured Creditors have been granted a lien or security interest pursuant to any of the Existing Security Documents or Watson Security Documents or this Agreement.

"Event of Default" means any Event of Default under and as defined in the Loan Agreement or Watson Security Documents.

"Existing Guaranty Agreements" means the guaranties and agreements identified on Schedule 1 hereto.

"Existing Holders" is defined in the Recitals hereto.

"Existing Intercreditor Agreement" means that certain Intercreditor Agreement, effective May 26, 1999, by and among Galen Partners III, L.P., Galen Partners International III, L.P., Galen Employee Fund III, L.P., and Oracle Strategic Partners, L.P.

"Existing Security Documents" means the guaranties, mortgages, deeds of trust and security agreements identified on Schedule 1 and Schedule 2 hereto.

"Grantors" means the Company, Halsey Pharmaceutical, Inc., a Delaware corporation and Houba Inc., an Indiana corporation, and each other subsidiary or affiliate of the Company that is or becomes a party to any Security Document.

"Guarantors" means Halsey Pharmaceutical, Inc., a Delaware corporation and Houba Inc., an Indiana corporation, and each other person that is or becomes a party to any Guaranty Agreement.

"Loan" is defined in the Recitals hereto.

"Loan Agreement" is defined in the Recitals hereto.

"Note" means that certain Secured Promissory Note, dated March __, 2000, executed by the Company in favor of Watson in the principal amount of \$17,500,000.

"Notice of Default" means a notice delivered by any Secured Creditor stating that an Event of Default has been declared and setting forth in reasonable detail the date and nature of such Event of Default.

"Secured Creditors" is defined in the Recitals hereto.

"Secured Obligations" is defined in the Recitals hereto.

"Senior Debt" means, at any time, the sum (without duplication) of the following:

(i) the aggregate principal amount of the Loan outstanding at such time and the aggregate amount of accrued unpaid interest thereon at such time; and

(ii) the reasonable costs and expenses of enforcement by Watson of its rights and collection with respect to the Loan.

"Subordinated Debt" means, at any time, the sum (without duplication) of the following:

(i) the aggregate principal amount of the Existing Debentures outstanding at such time and the aggregate amount of accrued unpaid interest thereon at such time;

(ii) the aggregate amount of accrued and unpaid fees payable to the Existing Holders, or any of them, under or in connection with the Existing Debentures; and

(iii) the aggregate amount of all other monetary obligations of the Company, the Guarantors and the Grantors that are accrued and owing at such time to the Existing Holders, or any of them, under the Existing Debentures (including all security, guaranty and other documents issued or executed in connection with and on the same date as the Existing Debentures) and the Existing Security Documents, including indemnification and expense reimbursement obligations thereunder.

"Watson Security Documents" means the guaranties, mortgages, deeds of trust and security agreements identified on Schedule 5.

SECTION 1.2. TERMS GENERALLY. The definitions in Section 1.1 shall apply equally to both the singular and plural forms of the terms defined. Whenever the context may require, any pronoun

shall include the corresponding masculine, feminine and neuter forms. The words "include," "includes" and "including" shall be deemed to be followed by the phrase "without limitation." All references herein to Articles and Sections shall be deemed references to Articles and Sections of this Agreement unless the context shall otherwise require.

ARTICLE II

STANDBY AND SUBORDINATION

Except as set forth in Article 3 of this Agreement, the Existing Holders shall not accept or receive, by setoff or in any other manner, as against the Company or the Guarantors, the whole or any part of the Subordinated Debt owing to the Existing Holders from the Company or the Guarantors, or any of their respective predecessors, successors or assigns, including, without limitation, a receiver, trustee or debtor in possession under the Existing Debentures or any note, guaranty or other instrument or agreement executed by the Company or the Guarantors in favor of the Existing Holders, or otherwise, whether the sums represent principal, interest, costs, attorneys' fees or charges, or other obligations due or not due, whether incurred directly or indirectly, and whether absolute or contingent unless and until the Senior Debt has been fully paid and satisfied.

ARTICLE III

PAYMENTS

So long as no Event of Default shall have occurred and be continuing under the Loan Agreement, the Company may pay to the Existing Holders, and the Existing Holders may accept or receive regularly scheduled payments in respect of the Subordinate Debt; provided, however, that the aggregate amount of payments (in any form) which may be made to and accepted by the Existing Holders shall not exceed the sum of Six Hundred and Twenty-Five Thousand Dollars (\$625,000) on any Interest Payment Date (as such term is defined in the Existing Debentures) and any arrearages thereon, and provided, further, however, that certain holders of the Existing Debentures designated on Schedule 4 attached hereto have agreed that, on each Interest Payment Date while any of the Senior Debt is outstanding, such holders shall receive such payments in the capital stock and/or like debenture instruments of Borrower and not in cash or cash equivalents. Watson shall provide notice to Oracle Strategic Partners, L.P., Galen Partners III, L.P., Galen Employee Fund III, L.P., and Galen Partners International III, L.P. of any Event of Default prior to its enforcement of its remedies hereunder, provided however, that nothing herein shall impair Watson's ability to act immediately after transmitting such notice. Except as to payments which the Existing Holders are permitted to accept or receive pursuant to this Article 3, the Existing Holders shall receive and hold all other payments or distributions received prior to the satisfaction of the Senior Debt in trust for the benefit of Watson and shall forthwith deliver the same to Watson in the same form received (except for the endorsement or assignment in favor of Watson where necessary) for application to the Senior Debt and, until so delivered, shall not be commingled with other funds or property of the Existing Holders. Upon any Event of Default under the Existing Debentures or the Support Documents, any Existing Holder may file, prosecute and obtain a judgment in a lawsuit against the Company or the Guarantors; provided, however, that the Existing Holders shall not commence foreclosure on any judgment lien obtained in connection therewith or otherwise exercise any remedy with respect thereto, including, without limitation, filing any petition in bankruptcy with respect to the Company or the Guarantors, unless and until all Senior Debt has been fully paid and satisfied.

ARTICLE IV

SECURITY INTEREST SUBORDINATION

All security interests acquired by Watson through the Watson Security Documents, to the extent securing the Senior Debt, in the Collateral shall at all times be prior and superior to any lien, ownership interest, security interest or other interest or claim now held or hereafter acquired by the Existing Holders in the Collateral (the "Subordinate Interest"). Said priority shall be applicable irrespective of the time or order of attachment or perfection of any security interest or the time or order of filing of any financing statements or other documents, or any statutes, rules of law, or court decisions to the contrary. Upon any disposition of any of the Collateral by Watson, the Existing Holders agree, if requested by Watson, to execute and immediately deliver any and all releases or other documents or agreements which Watson deems necessary to accomplish a disposition thereof free of the Subordinate Interest.

ARTICLE V

DISPOSITION OF COLLATERAL

The Existing Holders agree that, until Watson has received payment in full of all Senior Debt, Watson may dispose of, and exercise any other rights with respect to, any or all of the Collateral, free of the Subordinate Interest; provided, that the Existing Holders retain any rights they may have as a junior secured creditor with respect to the surplus, if any, arising from any such disposition or enforcement. The Existing Holders agree that any funds of the Company or the Guarantors which it obtains through the exercise of any right of setoff or other similar right constitute Collateral, and the Existing Holders shall immediately pay such funds to Watson to be applied to the outstanding Senior Debt.

ARTICLE VI

SENIOR DEBT

Until Watson has received payment in full of all Senior Debt, the Existing Holders agree that, in addition to any other rights that Watson may have, at law or in equity, Watson may at any time, and from time to time, without the Existing Holders' consent and without notice to the Existing Holders, renew or extend, but not increase, any of the Senior Debt or that of any other person at any time directly or indirectly liable for the payment of any Senior Debt, accept partial payments of the Senior Debt, settle, release (by operation of law or otherwise), compound, compromise, collect or liquidate any of the Senior Debt, change, alter or vary the interest charge on, or any other terms or provisions of the Senior Debt or any present or future instrument, document or agreement between the Senior Lender and the Company or the Guarantors, and take any other action or omit to take any other action with respect to the Senior Debt or the Collateral as Watson may deem necessary or advisable in its sole discretion. The Existing Holders waive any right to require Watson to marshal any assets in favor of the Existing Holders or against or in payment of any or all of the Senior Debt. The Existing Holders further waive any defense arising by reason of any claim or defense based upon an election of remedies by Watson which in any manner impairs, affects, reduces, releases, destroys and/or extinguishes any of the Existing Holders' subrogation rights, rights to proceed against the Company or the Guarantors for reimbursement, and/or any other rights of any of the Existing Holders.

ARTICLE VII

DEFAULT

The Existing Holders shall promptly give Watson written notice of any Event of Default by the Company or the Guarantors on any obligation secured by the Subordinate Interest.

ARTICLE VIII

NO COMMITMENT

It is understood and agreed that this Agreement shall in no way be construed as a commitment or agreement by Watson to continue financing arrangements with the Company or the Guarantors.

ARTICLE IX

NO CONTEST

The Existing Holders shall not contest the validity, perfection, priority or enforceability of any lien or security interest granted to Watson to secure the Senior Debt pursuant to the Watson Security Documents.

ARTICLE X

FINANCIAL CONDITION OF BORROWER

The Existing Holders are presently informed of the financial condition of the Company and of all other circumstances which a diligent inquiry would reveal and which bear upon the risk of non-payment of the Senior Debt and the Subordinated Debt. The Existing Holders acknowledge that they are each entitled to keep themselves informed under the terms of the Existing Debentures and the Existing Security Documents as to the Company's financial condition and all other circumstances which bear upon the risk of non-payment of the Senior Debt and the Subordinated Debt or the Existing Holders' compliance with their obligations hereunder. Except as otherwise specifically provided herein, the Existing Holders waive any right to require Watson to disclose to them any information which Watson may now or hereafter acquire concerning the Company or the Guarantors.

ARTICLE XI

REVIVOR

If any payment made on any of the Senior Debt shall for any reason be required to be returned by Watson, whether on the ground that such payment constituted a preference or for any other reason, then for purposes of this Agreement, such payment on the Senior Debt shall be treated as not having been made, and this Agreement shall in all respects be effective with respect to such Senior Debt as though such payment had not been made.

ARTICLE XII

REPRESENTATIONS AND WARRANTIES

SECTION 12.1. REPRESENTATIONS AND WARRANTIES OF THE EXISTING HOLDERS.

The Existing Holders represent and warrant that they have not heretofore transferred or assigned the Subordinate Interest or any financing statement naming any Grantor as debtor and any Existing Holder as secured party, and that they will not do so without first delivering a copy of this Agreement to the proposed transferee or assignee.

SECTION 12.2. REPRESENTATIONS AND WARRANTIES OF EACH PARTY. Each party

hereto represents and warrants to the other parties hereto that (a) the execution, delivery and performance of this Agreement (i) have been duly authorized by all requisite corporate action on its part and (ii) will not contravene any provision of its charter or by-laws or any order of any court or other governmental authority having applicability to it or any applicable law, and (b) this Agreement has been duly executed and delivered by it and constitutes its legal, valid and binding obligation.

ARTICLE XIII

EXISTING INTERCREDITOR AGREEMENT

The parties hereto acknowledge the existence of the Existing Intercreditor Agreement. Nothing herein shall be deemed to rescind any portion of the Existing Intercreditor Agreement and such agreement shall remain in full force except as modified by the terms of this Agreement.

ARTICLE XIV

MISCELLANEOUS

SECTION 14.1. NO INDIVIDUAL ACTION. No Secured Creditor may require any

other Secured Creditor to take or refrain from taking any action hereunder or under any of the Support Documents or with respect to any of the Collateral except as and to the extent expressly set forth in this Agreement.

SECTION 14.2. SUCCESSORS AND ASSIGNS. This Agreement shall be binding

on and inure to the benefit of each of the Secured Creditors and their respective successors and permitted assigns; provided, however, that, except as provided in the next sentence, no Existing Holder may assign its rights or obligations hereunder. The rights and obligations of any Existing Holder under this Agreement may be assigned, and the term "Existing Holder" as used in this Agreement shall include, any assignee, transferee or successor of such Existing Holder under the Existing Debentures by the execution of a Joinder Agreement by such assignee, transferee or successor, and any such assignee, transferee or successor shall thereupon become an Existing Holder under and a party to this Agreement. This Agreement is not intended to confer any benefit on, or create any obligation of any Secured Creditor to, the Company or any third party, including the Guarantors and other Grantors.

SECTION 14.3. NOTICES. Notices and other communications provided for

herein or in any Watson Security Document shall be in writing and shall be delivered by hand or overnight courier service, mailed or sent by telex or telecopy, as follows:

(a) if to any Existing Holder, to it as set forth opposite its signature on the signature pages hereto;

(b) if to Watson, to 311 Bonnie Circle, Corona, California, 91720, fax no. (909) 270-1096, to the attention of Mr. Robert Funsten, General Counsel; and

(c) if to the Company, to 695 No. Perryville Road, Rockford, Illinois 61107, fax no. (815) 399-9710, to the attention of Mr. Michael Reicher, Chief Executive Officer any Grantor, or any Guarantor, to it as specified in the Support Document to which it is a party.

(d) if to the other Grantors and Guarantors, as applicable to: (i) Houba, Inc., 16235 State Road, #17, Culver, Indiana 46511, fax no: _____, to the attention of Mr. Michael Reicher, Chief Executive Officer; or (ii) Halsey Pharmaceutical, Inc., 695 No. Perryville Road, Rockford, Illinois 61107, fax no. (815) 399-9710, to the attention of Mr. Michael Reicher, Chief Executive Officer. All notices and other communications given to any party hereto in accordance with the provisions of this Agreement shall be deemed to have been given on the date of receipt if delivered by hand or overnight courier service or sent by telex or telecopy, or on the date five Business Days after dispatch by certified or registered mail if mailed, in each case delivered, sent or mailed (properly addressed) to such party as provided in this Section 14.3 or in accordance with the latest unrevoked direction from such party given in accordance with this Section 14.3.

SECTION 14.4. TERMINATION. This Agreement shall terminate automatically upon the indefeasible payment in full of the Senior Debt.

SECTION 14.5. APPLICABLE LAW. THIS AGREEMENT SHALL BE CONSTRUED IN ACCORDANCE WITH AND GOVERNED BY THE LAWS OF THE STATE OF CALIFORNIA, WITHOUT REFERENCE TO ITS CHOICE OF LAW RULES.

SECTION 14.6. AMENDMENTS AND WAIVERS OF AGREEMENT AND SUPPORT DOCUMENTS. No amendment or waiver of any provision of this Agreement or any Support Document shall in any event be effective unless the same shall be in writing and signed by the Secured Creditors; provided, however, that no such amendment or waiver which materially affects the duties of the Company shall be effective without the prior written consent of the Company. No waiver of any provision of this Agreement and no consent to any departure by any party hereto from the provisions hereof shall be effective unless such waiver or consent shall be set forth in a written instrument executed by the party against which it is sought to be enforced, and then such waiver or consent shall be effective only in the specific instance and for the purpose for which given. No notice to or demand on any party hereto in any case shall entitle such party to any other or further notice or demand in the same, similar or other circumstances.

SECTION 14.7. WAIVER OF RIGHTS. Neither any failure nor any delay on the part of any party hereto in exercising any right, power or privilege hereunder shall operate as a waiver thereof, and a single or partial exercise thereof shall not preclude any other or further exercise or the exercise of any other right, power or privilege.

SECTION 14.8. SEVERABILITY. In case any one or more of the provisions contained in this Agreement should be invalid, illegal or unenforceable in any respect, the validity, legality and

enforceability of the remaining provisions contained herein shall not in any way be affected or impaired thereby. The parties shall endeavor in good faith negotiations to replace the invalid, illegal or unenforceable provisions with valid provisions the economic effect of which comes as close as possible to that of the invalid, illegal or unenforceable provision.

SECTION 14.9. WAIVER OF JURY TRIAL. NEITHER THE COMPANY, THE SECURED CREDITORS OR ANY GRANTOR OR GUARANTOR, NOR ANY ASSIGNEE, SUCCESSOR, HEIR OR PERSONAL REPRESENTATIVE OF THE COMPANY, ANY SECURED CREDITOR, OR ANY GRANTOR OR GUARANTOR SHALL SEEK A JURY TRIAL IN ANY LAWSUIT, PROCEEDING, COUNTERCLAIM OR ANY OTHER LITIGATION PROCEDURE BASED UPON OR ARISING OUT OF OR OTHERWISE RELATING TO THIS AGREEMENT, THE SUPPORT DOCUMENTS, ANY RELATED INSTRUMENT OR AGREEMENT, ANY COLLATERAL FOR ALL OR ANY PART OF THE LOAN AGREEMENT OBLIGATIONS OR EXISTING DEBENTURE OBLIGATIONS, OR THE DEALINGS OR THE RELATIONSHIP BETWEEN OR AMONG SUCH PERSONS. THE COMPANY, EACH SECURED CREDITOR AND EACH GRANTOR AND GUARANTOR HEREBY WAIVE ANY AND ALL RIGHT TO ANY SUCH JURY TRIAL. NEITHER THE COMPANY, ANY SECURED CREDITOR NOR ANY GRANTOR OR GUARANTOR SHALL SEEK TO CONSOLIDATE ANY SUCH ACTION IN WHICH A JURY TRIAL HAS BEEN WAIVED WITH ANY OTHER ACTION IN WHICH A JURY TRIAL CANNOT OR HAS NOT BEEN WAIVED. THE PROVISIONS OF THIS SECTION HAVE BEEN FULLY DISCUSSED BY THE PARTIES HERETO, AND THE PROVISIONS OF THIS AGREEMENT SHALL BE SUBJECT TO NO EXCEPTIONS. NO PARTY HAS IN ANY WAY AGREED WITH OR REPRESENTED TO ANY OTHER PARTY THAT THE PROVISIONS OF THIS SECTION WILL NOT BE FULLY ENFORCED IN ALL INSTANCES.

SECTION 14.10. COUNTERPARTS; EFFECTIVENESS. This Agreement may be executed in two or more counterparts, each of which shall constitute an original, but all of which, when taken together, shall constitute but one instrument. This Agreement shall become effective on the date (the "Closing Date") this Agreement shall have been executed and delivered by each party identified in the introductory paragraph hereto.

SECTION 14.11. SECTION HEADINGS. The Article and Section headings used herein are for convenience of reference only and are not to affect the construction of or be taken into consideration in interpreting this Agreement.

SECTION 14.12. COMPLETE AGREEMENT. This Agreement constitutes the entire agreement between the parties hereto with respect to the subject matter hereof and supersedes all prior representations, negotiations, writings, memoranda and agreements. To the extent any provision of this Agreement conflicts with any of the documents referenced herein, the provisions of this Agreement shall be controlling.

[signature pages to follow]

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

"WATSON"

WATSON PHARMACEUTICAL, INC.,
a Nevada corporation

/s/ Robert C. Funsten

By:
Its: Senior Vice President

"GRANTOR/GUARANTOR"

HOUBA, INC.,
an Indiana corporation

/s/ Michael Reicher

By:
Its: Chief Executive Officer

ORACLE STRATEGIC PARTNERS, L.P.
By: Oracle Strategic Capital L.L.C.,
General Partner
712 Fifth Avenue
New York, New York 10019

/s/ Larry Feinberg

By:
Its: Managing Member

GALEN EMPLOYEE FUND III, L.P.
By: Wesson Enterprises, Inc.
610 Fifth Avenue, 5th Floor
New York, New York 10020

/s/ Bruce F. Wesson

By:
Its: General Partner

"THE COMPANY"

HALSEY DRUG CO., INC.,
a New York corporation

/s/ Michael Reicher

By:
Its: Chief Executive Officer

"GRANTOR/GUARANTOR"

HALSEY PHARMACEUTICAL, INC.,
a Delaware corporation

/s/ Michael Reicher

By:
Its: Chief Executive Officer

GALEN PARTNERS III, L.P.
By: Claudius, L.L.C., General Partner
610 Fifth Avenue, 5th Fl.
New York, New York 10019

/s/ Shrini Conjeevaram

By:
Its: General Partner

GALEN PARTNERS INTERNATIONAL, III, L.P.
By: Claudius, L.L.C., General Partner
610 Fifth Avenue, 5th Floor
New York, New York 10020

/s/ Shrini Conjeevaram

By:
Its: General Partner

ALAN SMITH
21 Bedlow Avenue
Newport, Rhode Island 02840

/s/ Alan Smith

MICHAEL WEISBROT
1136 Rock Creek Road
Gladwyne, Pennsylvania 19035

/s/ Michael Weisbrot

GREG WOOD
c/o D.R. International
7474 No. Figueroa Street
Los Angeles, California 90041

/s/ Greg Wood

BERNARD SELZ
c/o Furman Selz
230 Park Avenue
New York, New York 10069

/s/ Bernard Selz

MICHAEL REICHER
c/o Halsey Drug Co., Inc.
695 North Perryville Rd.
Crimson Building #2
Rockford, Ill. 61107

/s/ Michael K. Reicher

PATRICK COYNE
477 Margo Lane
Berwyn, Pennsylvania 19312

/s/ Patrick Coyne

SUSAN WEISBROT
1136 Rock Creek Road
Gladwyne, Pennsylvania 19035

/s/ Susan Weisbrot

DENNIS ADAMS
120 Kynlyn Road
Radnor, Pennsylvania 19312

/s/ Dennis Adams

ROBERT W. BAIRD & CO., INC., TTEE
FBO Michael K. Reicher IRA
c/o Halsey Drug Co., Inc.
695 North Perryville Rd.
Crimson Building #2
Rockford, Ill. 61107

/s/ Michael K. Reicher

By:
Its: Trustee

PETER CLEMENS
c/o Halsey Drug Co., Inc.
695 North Perryville Rd.
Crimson Building #2
Rockford, Ill. 61107

/s/ Peter Clemens

CONNIE REICHER TRUST
c/o Halsey Drug Co., Inc.
695 North Perryville Rd.
Crimson Building #2
Rockford, Ill. 61107

/s/ Connie Reicher

By:
Its: Trustee

DAN HILL
6725 Lynch Avenue
Riverbank, California 95367

/s/ Dan Hill

VARSHA H. SHAH
29 Chrissy Drive
Warren, New Jersey 07059

/s/ Varshah H. Shah

VARSHA H. SHAH AS CUSTODIAN
FOR SACHIN H. SHAH
29 Chrissy Drive
Warren, New Jersey 07059

/s/ Varshah H. Shah

By:
Its: Custodian

MICHAEL RAINISCH
c/o Alvin Rainisch
315 Devon Place
Morganville, New Jersey 07751

/s/ Michael Rainisch

STEFANIE HEITMEYER
c/o Halsey Drug Co., Inc.
695 North Perryville Rd.
Crimson Building #2
Rockford, Ill. 61107

/s/ Stefanie Heitmeyer

HEMANT K. SHAH
29 Chrissy Drive
Warren, New Jersey 07059

/s/ Hemant K. Shah

VARSHA H. SHAH AS CUSTODIAN
FOR SUMEET H. SHAH
29 Chrissy Drive
Warren, New Jersey 07059

/s/ Varshah H. Shah

By:
Its: Custodian

ILENE RAINISCH
c/o Alvin Rainisch
315 Devon Place
Morganville, New Jersey 07751

/s/ Ilene Rainisch

KENNETH GIMBEL
2455 Montgomery Avenue
Highland Park, Ill. 60035

/s/ Kenneth Gimbel

KENNETH GIMBEL, IRA ACCOUNT
FBO KENNETH GIMBEL
2455 Montgomery Avenue
Highland Park, Ill. 60035

- - - - -
By:
Its:

SCHEDULE 1

LIST OF EXISTING GUARANTY AGREEMENTS

1. Continuing Unconditional Secured Guaranty by Houba, Inc. dated March 10, 1998.
2. Continuing Unconditional Secured Guaranty by Halsey Pharmaceutical, Inc. dated March 10, 1998.
3. Continuing Unconditional Secured Guaranty by Houba, Inc. dated May 26, 1999.
4. Continuing Unconditional Secured Guaranty by Halsey Pharmaceutical, Inc. dated May 26, 1999.

SCHEDULE 1

SCHEDULE 2

LIST OF EXISTING SECURITY DOCUMENTS

1. Company General Security Agreement, dated March 10, 1998, between Halsey Drug Co., Inc. and Galen Partners III, L.P., as agent.
2. Guarantors General Security Agreement, dated March 10, 1998, by and among Cenci Powder Products, Inc., Halsey Pharmaceutical, Inc., H.R. Cenci Laboratories, Inc., Houba, Inc., Indiana Fine Chemicals, Inc. and Galen Partners III, L.P., as agent.
3. Stock Pledge Agreement, dated March 10, 1998, between Halsey Drug Co., Inc. and Galen Partners III, L.P., as agent.
4. Company General Security Agreement, dated March 26, 1999, between Halsey Drug Co., Inc. and Oracle Strategic Partners, L.P., as agent.
5. Guarantors General Security Agreement dated, May 26, 1999, by and among Houba, Inc., Halsey Pharmaceutical, Inc. and Oracle Strategic Partners, L.P., as agent.
6. Stock Pledge Agreement, dated May 26, 1999, between Halsey Drug Co., Inc. and Oracle Strategic Partners, L.P., as agent.

SCHEDULE 2

SCHEDULE 3

EXISTING MORTGAGES AND DEEDS OF TRUST

1. Real estate mortgage, dated May 10, 1998, between Houba, Inc. and Galen Partners III, L.P., as agent, covering the property located at 16235 State Road 17, Culver, Indiana 46511.
2. Real estate mortgage, dated May 26, 1999, between Houba, Inc. and Oracle Strategic Partners, L.P., as agent, covering the property located at 16235 State Road 17, Culver, Indiana 46511.

SCHEDULE 3

SCHEDULE 4
EXISTING HOLDERS

GALEN DEBENTURES

Name and Address of Purchaser - - - - -	Principal Amount of Debenture Purchased - - - - -	\$1.50 Warrants - - - - -	\$2.375 Warrants - - - - -
Galen Partners III, L.P.* 610 Fifth Avenue, 5th Floor New York, New York 10020	\$ 15,423,195	1,557,898	1,557,898
Galen Partners International III, L.P.* 610 Fifth Avenue, 5th Floor New York, New York 10020	\$ 1,709,167	172,643	172,643
Galen Employee Fund III, L.P.* 610 Fifth Avenue, 5th Floor New York, New York 10020	\$ 67,638	6,833	6,833
Michael Reicher* c/o Halsey Drug Co., Inc. 1827 Pacific Street Brooklyn, New York 11233	\$ 300,000	30,303	30,303
Peter Clemens* c/o Halsey Drug Co., Inc. 1827 Pacific Street Brooklyn, New York 11233	\$ 100,000	10,101	10,101
Stefanie Heitmeyer c/o Halsey Drug Co., Inc. 1827 Pacific Street Brooklyn, New York 11233	\$ 20,000	2,020	2,020
Dan Hill c/o Halsey Drug Co., Inc. 1827 Pacific Street Brooklyn, New York 11233	\$ 10,000	1,010	1,010

Name and Address of Purchaser - - - - -	Purchase Price - - - - -
Galen Partners III, L.P.* 610 Fifth Avenue, 5th Floor New York, New York 10020	\$ 15,423,195
Galen Partners International III, L.P.* 610 Fifth Avenue, 5th Floor New York, New York 10020	\$ 1,709,167
Galen Employee Fund III, L.P.* 610 Fifth Avenue, 5th Floor New York, New York 10020	\$ 67,638
Michael Reicher* c/o Halsey Drug Co., Inc. 1827 Pacific Street Brooklyn, New York 11233	\$ 300,000
Peter Clemens* c/o Halsey Drug Co., Inc. 1827 Pacific Street Brooklyn, New York 11233	\$ 100,000
Stefanie Heitmeyer	\$ 20,000

c/o Halsey Drug Co., Inc.
1827 Pacific Street
Brooklyn, New York 11233

Dan Hill	\$	10,000
c/o Halsey Drug Co., Inc.		
1827 Pacific Street		
Brooklyn, New York 11233		

*Agrees to receive interest in capital stock or like kind debentures.

SCHEDULE 4

Name and Address of Purchaser - - - - -	Principal Amount of Debenture Purchased -----	\$1.50 Warrants -----	\$2.375 Warrants -----
Alan Smith c/o Halsey Drug Co., Inc. 1827 Pacific Street Brooklyn, New York 11233	\$ 10,000	1,010	1,010
Dennis Adams 120 Kynlyn Road Radnor, Pennsylvania 19087	\$ 1,170,000	118,182	118,182
Patrick Coyne 477 Margo Lane Berwyn, Pennsylvania 19312	\$ 50,000	5,051	5,051
Michael Weisbrot and Susan Weisbrot 1136 Rock Creek Road Gladwyne, Pennsylvania 19035	\$ 300,000	30,303	30,303
Greg Wood 1263 East Calaveras Street Altadena, California 91001	\$ 100,000	10,101	10,101
Hemant K. Shah and Varsha H. Shah 29 Christy Drive Warren, New Jersey 07059	\$ 950,000	95,960	95,960
Varsha H. Shah as Custodian for Sumeet H. Shah 29 Christy Drive Warren, New Jersey 07059	\$ 20,000	2,020	2,020
Varsha H. Shah as Custodian for Sachin H. Shah 29 Christy Drive Warren, New Jersey 07059	\$ 20,000	2,020	2,020
Bernard Selz 121 East 73rd Street New York, New York 10021	\$ 400,000	40,404	40,404

Name and Address of Purchaser - - - - -	Purchase Price -----
Alan Smith c/o Halsey Drug Co., Inc. 1827 Pacific Street Brooklyn, New York 11233	\$ 10,000
Dennis Adams 120 Kynlyn Road Radnor, Pennsylvania 19087	\$ 1,170,000
Patrick Coyne 477 Margo Lane Berwyn, Pennsylvania 19312	\$ 50,000
Michael Weisbrot and Susan Weisbrot 1136 Rock Creek Road Gladwyne, Pennsylvania 19035	\$ 300,000
Greg Wood 1263 East Calaveras Street Altadena, California 91001	\$ 100,000
Hemant K. Shah and Varsha H. Shah 29 Christy Drive Warren, New Jersey 07059	\$ 950,000
Varsha H. Shah as Custodian for Sumeet H. Shah 29 Christy Drive Warren, New Jersey 07059	\$ 20,000
Varsha H. Shah as Custodian for Sachin H. Shah	\$ 20,000

29 Christy Drive
Warren, New Jersey 07059

Bernard Selz 121 East 73rd Street New York, New York 10021	\$	400,000
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*Agrees to receive interest in capital stock or like kind debentures.

SCHEDULE 4

Name and Address of Purchaser -----	Principal Amount of Debenture Purchased -----	\$1.50 Warrants -----	\$2.375 Warrants -----
Ilene Rainisch 315 Devon Place Morganville, New Jersey 07751	\$ 25,000	2,525	2,525
Michael Rainisch 48 Radford Street Staten Island, New York 10314	\$ 25,000	2,525	2,525
Ken Gimbel 876 Kimball Road Highland Park, Illinois 60035	\$ 100,000	10,101	10,101

Name and Address of Purchaser -----	Purchase Price -----
Ilene Rainisch 315 Devon Place Morganville, New Jersey 07751	\$ 25,000
Michael Rainisch 48 Radford Street Staten Island, New York 10314	\$ 25,000
Ken Gimbel 876 Kimball Road Highland Park, Illinois 60035	\$ 100,000

*Agrees to receive interest in capital stock or like kind debentures.

SCHEDULE 4

Name and Address of Purchaser -----	Debenture Number and Corresponding Principal Amount -----	\$1.50 Warrants -----	\$2.375 Warrants -----	Purchase Price -----
Galen Partners III, L.P.* 610 Fifth Avenue, 5th Floor New York, New York 10020	No. N-19A \$681,105	68,798	68,798	\$ 681,105
Galen Partners International III, L.P.* 610 Fifth Avenue, 5th Floor New York, New York 10020	No. N-38 \$3,073,704	310,476	310,476	\$ 3,073,704
Galen Employee Fund III, L.P.* 610 Fifth Avenue, 5th Floor New York, New York 10020	No. N-20 \$65,913	6,658	6,658	\$ 65,913
	No. N-39 \$297,456	30,044	30,044	\$ 297,456
	No. N-21 \$2,982	301	301	\$ 2,982
	No. N-40 \$13,456	1,361	1,361	\$ 13,456
Michael Reicher* c/o Halsey Drug Co., Inc. 1827 Pacific Street Brooklyn, New York 11233	No. N-22 \$50,000	5,026	5,026	\$ 50,000
Robert W. Baird & Co., Inc. TTEE, FBO Michael K. Reicher IRA, Account Number 7026-6907 c/o Halsey Drug Co., Inc. 1827 Pacific Street Brooklyn, New York 11233	No. N-22A \$22,115	2,258	2,258	\$ 22,115
Peter Clemens* c/o Halsey Drug Co., Inc. 1827 Pacific Street Brooklyn, New York 11233	No. N-23 \$24,038	2,428	2,428	\$ 24,038

*Agrees to receive interest in capital stock or like kind debentures.

SCHEDULE 4

Name and Address of Purchaser -----	Debenture Number and Corresponding Principal Amount -----	\$1.50 Warrants -----	\$2.375 Warrants -----	Purchase Price -----
Stefanie Heitmeyer c/o Halsey Drug Co., Inc. 1827 Pacific Street Brooklyn, New York 11233	No. N-24 \$4,808	486	486	\$ 4,808
Dan Hill c/o Halsey Drug Co., Inc. 1827 Pacific Street Brooklyn, New York 11233	No. N-25 \$2,404	243	243	\$ 2,404
Alan Smith c/o Halsey Drug Co., Inc. 1827 Pacific Street Brooklyn, New York 11233	No. N-29 \$2,404	243	243	\$ 2,404
Dennis Adams 120 Kynlyn Road Radnor, Pennsylvania 19087	No. N-31 \$281,250	28,409	28,409	\$ 281,250
Patrick Coyne 477 Margo Lane Berwyn, Pennsylvania 19312	No. N-32 \$12,019	1,214	1,214	\$ 12,019
Michael Weisbrot and Susan Weisbrot 1136 Rock Creek Road Gladwyne, Pennsylvania 19035	No. N-33 \$72,115	7,284	7,284	\$ 72,115
Greg Wood 1263 East Calaveras Street Altadena, California 91001	No. N-26 \$24,038	2,428	2,428	\$ 24,038
Hemant K. Shah and Varsha H. Shah 29 Christy Drive Warren, New Jersey 07059	No. N-34 \$228,365	23,067	23,067	\$ 228,365
Varsha H. Shah as Custodian for Sumeet H. Shah 29 Christy Drive Warren, New Jersey 07059	No. N-35 \$4,808	486	486	\$ 4,808

*Agrees to receive interest in capital stock or like kind debentures.

SCHEDULE 4

Name and Address of Purchaser -----	Debenture Number and Corresponding Principal Amount -----	\$1.50 Warrants -----	\$2.375 Warrants -----	Purchase Price -----
Varsha H. Shah as Custodian for Sachin H. Shah 29 Christy Drive Warren, New Jersey 07059	No. N-36 \$4,808	486	486	\$ 4,808
Bernard Selz 121 East 73rd Street New York, New York 10021	No. N-37 \$96,154	9,712	9,712	96,154
Ilene Rainisch 315 Devon Place Morganville, New Jersey 07751	No. N-27 \$6,010	607	607	\$ 6,010
Michael Rainisch 48 Radford Street Staten Island, New York 10314	No. N-28 \$6,010	607	607	\$ 6,010
Ken Gimbel 876 Kimball Road Highland Park, Illinois 60035	No. N-30 \$24,038	2,428	2,428	\$ 24,038

*Agrees to receive interest in capital stock or like kind debentures.

SCHEDULE 4

EXISTING HOLDERS

ORACLE DEBENTURES

Oracle Debentures Name and Address of Purchaser -----		Principal Amount of Debenture Purchased -----	\$1.404 Warrants -----	\$2.285 Warrants -----
1.	Oracle Strategic Partners, L.P.*	\$ 5,000,000.00	505,050	505,050
2.	Oracle Strategic Partners, L.P.*	\$ 5,000,000.00(1)	1,010,100	1,010,100
3.	Galen Partners III, L.P.*	\$ 5,964,583.09(2)	602,483	602,483
4.	Galen Partners International III, L.P.*	\$ 539,900.40(3)	54,535	54,535
5.	Galen Employee Fund III, L.P.*	\$ 24,424.10(4)	2,467	2,467
6.	Patrick Coyne	\$ 51,178.08(5)	5,169	5,169
7.	Alan Smith	\$ 13,358.08(6)	1,349	1,349
8.	Michael and Susan Weisbrot	\$ 564,446.96(7)	57,015	57,015
9.	Greg Wood	\$ 204,712.33(8)	20,678	20,678
10.	Dennis Adams	\$ 300,000.00	30,303	30,303
11.	Bernard Selz	\$ 200,000.00	20,202	20,202
Total		\$ 17,862,603.04	2,309,351.00	2,309,351.00

Oracle Debentures Name and Address of Purchaser -----		Purchase Price -----
1.	Oracle Strategic Partners, L.P.*	\$ 5,000,000.00
2.	Oracle Strategic Partners, L.P.*	\$ 5,000,000.00
3.	Galen Partners III, L.P.*	\$ 5,964,583.09
4.	Galen Partners International III, L.P.*	\$ 539,900.40
5.	Galen Employee Fund III, L.P.*	\$ 24,424.10
6.	Patrick Coyne	\$ 51,178.08
7.	Alan Smith	\$ 13,358.08
8.	Michael and Susan Weisbrot	\$ 564,446.96
9.	Greg Wood	\$ 204,712.33
10.	Dennis Adams	\$ 300,000.00
11.	Bernard Selz	\$ 200,000.00
Total		\$ 17,862,603.04

- 1 Intentionally omitted.
- 2 Consists of the surrender of convertible bridge notes in the principal amount of \$5,590,917 plus accrued and unpaid interest of \$373,666.09.
- 3 Consists of the surrender of convertible bridge notes in the principal amount of \$506,077 plus accrued and unpaid interest of \$33,823.40.
- 4 Consists of the surrender of convertible bridge notes in the principal amount of \$22,894 plus accrued and unpaid interest of \$1,530.10.
- 5 Consists of (i) the surrender of convertible bridge notes in the principal amount of \$25,000 plus accrued and unpaid interest of \$1,178.08 and (ii) an additional investment of \$25,000.
- 6 Consists of the surrender of convertible bridge notes in the principal amount of \$13,000 plus accrued and unpaid interest of \$358.08.

- 7 Consists of (i) the surrender of convertible bridge notes in the principal amount of \$351,222 plus accrued and unpaid interest of \$13,224.96 and (ii) an additional investment of \$200,000.
- 8 Consists of (i) the surrender of convertible bridge notes in the principal amount of \$100,000 plus accrued and unpaid interest of \$4,712.33 and (ii) an additional investment of \$100,000.

*Agrees to receive interest in capital stock or like kind debentures.

SCHEDULE 4

EXHIBIT A
FORM OF
JOINDER AGREEMENT

Reference is made to that certain Subordination Agreement, dated as of March __, 2000 (the "Subordination Agreement"), by and among Watson Pharmaceuticals, Inc., a Nevada corporation, Halsey Drug Co., Inc., a New York corporation ("Halsey"), Galen Partners III, L.P., as Agent of the holders of the Galen Debentures, the Oracle Investor Group and the Grantors and Guarantors listed on the signature pages thereof. All capitalized terms used but not defined herein have the respective meanings ascribed thereto in the Subordination Agreement. This agreement is a Joinder Agreement referred to in Section 14.2 of the Subordination Agreement.

The undersigned hereby agrees that it is a party to the Subordination Agreement and is therefore bound by, and subject to, the terms of the Subordination Agreement, and that it is an "Existing Holder" under, and as defined, therein.

The undersigned certifies that on or about the date hereof it is the holder of the following obligations of the Company outstanding under the Existing Debentures, as applicable.

[describe obligations]

The address for notices to the undersigned pursuant to the Subordination Agreement is as follows:

[set forth address for notices]

Very truly yours,

[CREDITOR]

By _____

Name:

Title:

EXHIBIT A

SCHEDULE 5

WATSON SECURITY DOCUMENTS

Watson Security Agreement

Watson Stock Pledge Agreement

Watson Guaranty

Watson Guarantors Security Agreement

Deed of Trust on Culver, Indiana Property

Deed of Trust Subordination

EXHIBIT A

YOURS TRULY, _____ STATE OF INDIANA _____ SPACE ABOVE THIS LINE
FOR RECORDING DATA

REAL ESTATE MORTGAGE
(With Future Advance Clause)

1. DATE AND PARTIES. The date of this Real Estate Mortgage ("Security Instrument") is March 29, 2000 and the parties, their addresses and tax identification numbers, if required, are as follows:

MORTGAGOR: Houba, Inc.
16235 State Road 17
Culver, Indiana 46511
Tax ID#: 35-1356439

[] If checked, refer to the attached Addendum incorporated herein, for additional Mortgagors, their signatures and acknowledgments.

LENDER: Watson Pharmaceuticals, Inc.
311 Bonnie Circle
Corona, California 91720

2. CONVEYANCE. For good and valuable consideration, the receipt and sufficiency of which is acknowledged, and to secure the Secured Debt (defined below) and Mortgagor's performance under this Security Instrument, Mortgagor grants, bargains, conveys, mortgages and warrants to Lender the following described property:

See Exhibit A attached hereto.

The property is located in Marshall County at 16235 State Road 17, Culver, Indiana 46511, together with all rights, easements, appurtenances, royalties, mineral rights, oil and gas rights, crops, timber, all diversion payments or third party payments made to crop producers, all water and riparian rights, wells, ditches, reservoirs, and water stock and all existing and future improvements, structures, fixtures, and replacements that may now, or at any time in the future, be part of the real estate described above (all referred to as the "Property").

3. MAXIMUM OBLIGATION LIMIT. The total principal amount secured by this Security Instrument at any one time shall not exceed \$17,500,000.00. This limitation of amount does not include interest and other fees and charges validly made pursuant to this Security Instrument. Also, this limitation does not apply to advances made under the terms of this Security Instrument to protect Lender's security and to perform any of the covenants contained in this Security Instrument.

4. SECURED DEBT AND FUTURE ADVANCES. The term "Secured Debt" is defined as follows:

- A. Debt incurred under the terms of all promissory note(s), contract(s), guaranty(s) or other evidence of debt described below and all their extensions, renewals, modifications or substitutions. (When referencing the debts below it is suggested that you include items such as borrowers' names, note amounts, interest rates, maturity dates, etc.)

See Exhibit B attached hereto.

- B. All future advances from Lender to Mortgagor or other future obligations of Mortgagor to Lender under any promissory note, contract, guaranty or other evidence of debt existing now or executed after this Security Instrument whether or not this Security Instrument is specifically referenced. If more than one person signs this Security Instrument, each Mortgagor agrees that this Security Instrument will secure all future advances and future obligations that are given to or incurred by any one or more Mortgagor, or any one or more Mortgagor and others. All future advances and other future obligations are secured by this Security Instrument even though all or part may not yet be advanced. All future advances and other future obligations are secured as if made on the date of this Security Instrument. Nothing in this Security Instrument shall constitute a commitment to make additional or future loans or advances in any amount. Any such commitment must be agreed to in a separate writing.
- C. All obligations that Mortgagor owes to Lender, which now exist or may later, arise, to the extent not prohibited by law, including, but not limited to, liabilities for overdrafts relating to any deposit account agreement between Mortgagor and Lender.
- D. All additional sums advanced and expenses incurred by Lender for insuring, preserving or otherwise protecting the Property and its value and any other sums advanced and expenses incurred by Lender under the terms of this Security Instrument.

This Security Instrument will not secure any other debt if Lender fails to give any required notice of the right of rescission.

5. PAYMENTS. Mortgagor agrees that all payments under the Secured Debt will be paid when due and in accordance with the terms of the Secured Debt and this Security Instrument.

6. WARRANTY OF TITLE. Mortgagor warrants that Mortgagor is or will be lawfully seized of the estate conveyed by this Security Instrument and has the right to grant, bargain, convey, sell, mortgage and warrant the Property. Mortgagor also warrants that the Property is unencumbered, except for encumbrances of record.

7. OTHER SECURITY INTERESTS. With regard to any other mortgage, deed of trust, security agreement or other lien document that created a prior or subsequent security interest or encumbrance on the Property, Mortgagor agrees:

- A. To make all payments when due and to perform or comply with all covenants.

B. To promptly deliver to Lender any notices that Mortgagor receives from the holder.

C. Not to allow any modification or extension of, nor to request any future advances under any note or agreement secured by the lien document without Lender's prior written consent.

8. CLAIMS AGAINST TITLE. Mortgagor will pay all taxes, assessments, liens, encumbrances, lease payments, ground rents, utilities, and other charges relating to the Property when due. Lender may require Mortgagor to provide to Lender copies of all notices that such amounts are due and the receipts evidencing Mortgagor's payment. Mortgagor will defend title to the Property against any claims that would impair the lien of this Security Instrument. Mortgagor agrees to assign to Lender, as requested by Lender, any rights, claims or defenses that Mortgagor may have against parties who supply labor or materials to maintain or improve the Property.

9. DUE ON SALE OR ENCUMBRANCE. Lender may, at its option, declare the entire balance of the Secured Debt to be immediately due and payable upon the creation of, or contract for the creation of, any lien, encumbrance, transfer or sale of the Property. This right is subject to the restrictions imposed by federal law (12 C.F.R. 591), as applicable. This covenant shall run with the Property and shall remain in effect until the Secured Debt is paid in full and this Security Instrument is released.

10. TRANSFER OF AN INTEREST IN THE MORTGAGOR. If Mortgagor is an entity other than a natural person (such as a corporation or other organization), Lender may demand immediate payment if:

A. A beneficial interest in Mortgagor is sold or transferred.

B. There is a change in either the identity or number of members of a partnership or similar entity.

C. There is a change in ownership of more than twenty-five percent (25%) of the voting stock of a corporation or similar entity.

However, Lender may not demand payment in the above situations if it is prohibited by law as of the date of this Security Instrument.

11. ENTITY WARRANTIES AND REPRESENTATIONS. If Mortgagor is an entity other than a natural person (such as a corporation or other organization), Mortgagor makes to Lender the following warranties and representations which shall continue as long as the Secured Debt remains outstanding:

A. Mortgagor is duly organized and validly existing in Mortgagor's state of incorporation or organization. Mortgagor is in good standing in all states in which Mortgagor transacts business. Mortgagor has the power and authority to own the Property and to carry on its business as now being conducted and, as applicable, is qualified to do so in each state in which Mortgagor operates.

B. The execution, delivery and performance of this Security Instrument by Mortgagor and the obligations evidenced by the Secured Debt are within the

power of Mortgagor, have been duly authorized, have received all necessary governmental approval, and will not violate any provision of law, or order of court or governmental agency.

- C. Other than previously disclosed in writing to Lender, Mortgagor has not changed its name within the last ten (10) years and has not used any other trade or fictitious name. Without Lender's prior written consent, Mortgagor does not and will not use any other name and will preserve its existing name, trade names and franchises until the Secured Debt is satisfied.

12. PROPERTY CONDITION, ALTERATIONS AND INSPECTION. Mortgagor will keep the Property in good condition and make all repairs that are reasonably necessary. Mortgagor shall not commit or allow any waste, impairment, or deterioration of the Property. Mortgagor will keep the Property free of noxious weeds and grasses. Mortgagor agrees that the nature of the occupancy and use will not substantially change without Lender's prior written consent. Mortgagor will not permit any change in any license, restrictive covenant or easement without Lender's prior written consent. Mortgagor will notify Lender of all demands, proceeds, claims, and actions against Mortgagor, and of any loss or damage to the Property.

No portion of the Property will be removed, demolished or materially altered without Lender's prior written consent except that Mortgagor has the right to remove items of personal property comprising a part of the Property that become worn or obsolete, provided that such personal property is replaced with other personal property at least equal in value and quality to the replaced personal property, free from any title retention device, security agreement or other encumbrance. Such replacement to personal property will be deemed subject to the security interest created by this Security Instrument. Mortgagor shall not partition or subdivide the Property without Lender's prior written consent.

Lender or Lender's agents may, at Lender's option, enter the Property at any reasonable time for the purpose of inspecting the Property. Lender shall give Mortgagor notice at the time of or before an inspection specifying a reasonable purpose for the inspection. Any inspection of the Property shall be entirely for Lender's benefit and Mortgagor will in no way rely on Lender's inspection.

13. AUTHORITY TO PERFORM. If Mortgagor fails to perform any duty or any of the covenants contained in this Security Instrument, Lender may, without notice, or obligation to do so, perform or cause them to be performed. Mortgagor appoints Lender as attorney-in-fact to sign Mortgagor's name or pay any amount necessary for performance. Lender's right to perform for Mortgagor shall not create an obligation to perform, and Lender's failure to perform will not preclude Lender from exercising any of Lender's other rights under the law or this Security Instrument. If any construction on the Property is discontinued or not carried on in a reasonable manner, Lender may take all steps necessary to protect Lender's security interest in the Property, including completion of the construction.

14. ASSIGNMENT OF LEASES AND RENTS. Mortgagor grants, bargains, conveys and warrants to Lender, as additional security, all right, title and interest in and to any and all:

- A. Existing or future leases, subleases, licenses, guaranties and any other written or verbal agreements for the use and occupancy of any portion of the

Property, including any extensions, renewals, modifications or substitutions of such agreements (all referred to as "Leases").

- B. Rents, issues and profits (all referred to as "Rents"), including, but not limited to, security deposits, minimum rent, percentage rent, additional rent, common area maintenance charges, parking charges, real estate taxes, other applicable taxes, insurance premium contributions, liquidated damages following default, cancellation premiums, "loss of rents" insurance, guest receipts, revenues, royalties, proceeds, bonuses, accounts, contract rights, general intangibles, and all rights and claims which Mortgagor may have that in any way pertain to or are on account of the use or occupancy of the whole or any part of the Property.

In the event any item listed as Leases or Rents is determined to be personal property, this Security Instrument will also be regarded as a security agreement.

Mortgagor will promptly provide Lender with true and correct copies of all existing and future Leases.

Mortgagor may collect, receive, enjoy and use the Rents so long as Mortgagor is not in default.

Mortgagor will not collect any Rents due in future lease periods, unless Mortgagor first obtains Lender's written consent. Upon default, Mortgagor will receive any Rents in trust for Lender and Mortgagor will not commingle the Rents with any other funds. Any amounts collected shall be applied at Lender's discretion to payments on the Secured Debt as therein provided, to costs of managing the Property, including, but not limited to, all taxes, assessments, insurance premiums, repairs, and commissions to rental agents, and to any other necessary related expenses including Lender's attorneys' fees and costs.

Mortgagor acknowledges that this assignment is immediately effective between the parties to this assignment and effective as to third parties on the recording of this Security Instrument. Mortgagor agrees that Lender is entitled to notify Mortgagor or Mortgagor's tenants to make payments of Rents due or to become due directly to Lender after such recording, however Lender agrees not to notify Mortgagor's tenants until Mortgagor defaults and Lender notifies Mortgagor of the default and demands that Mortgagor and Mortgagor's tenants pay all Rents due or to become due directly to Lender. Immediately after Lender gives Mortgagor the notice of default, Mortgagor agrees that either Lender or Mortgagor may immediately notify the tenants and demand that all future Rents be paid directly to Lender. On receiving the notice of default, Mortgagor will endorse and deliver to Lender any payments of Rents. If Mortgagor becomes subject to a voluntary or involuntary bankruptcy, then Mortgagor agrees that Lender is entitled to receive relief from the automatic stay in bankruptcy for the purpose of making this assignment effective and enforceable under state and federal law and within Mortgagor's bankruptcy proceedings.

Mortgagor warrants that no default exists under the Leases or any applicable law. Mortgagor also agrees to maintain, and to require the tenants to comply with, the Leases and any applicable law. Mortgagor will promptly notify Lender of any noncompliance. If Mortgagor neglects or refuses to enforce compliance with the terms of the Leases, then Lender may, at Lender's option, enforce compliance. Mortgagor will obtain Lender's written authorization before Mortgagor consents to

sublet, modify, cancel, or otherwise alter the Leases, to accept the surrender of the Property covered by such Leases (unless the Leases so require), or to assign, compromise or encumber the Leases or any future Rents. If Lender acts to manage, protect and preserve the Property, Lender does not assume or become liable for its maintenance, depreciation, or other losses or damages, except those due to Lender's gross negligence or intentional torts. Otherwise, Mortgagor will hold Lender harmless and indemnify Lender for any and all liability, loss or damage that Lender may incur as a consequence of the assignment under this section.

15. LEASEHOLDS; CONDOMINIUMS; PLANNED UNIT DEVELOPMENTS. Mortgagor agrees to comply with the provisions of any lease if this Security Instrument is on a leasehold. If the Property includes a unit in a condominium or a planned unit development, Mortgagor will perform all of Mortgagor's duties under the covenants, by-laws, or regulations of the condominium or planned unit development.

16. DEFAULT. Mortgagor will be in default if any of the following shall occur:

- A. Any party obligated on the Secured Debt fails to make payment when due;
- B. A breach of any term or covenant in this Security Instrument or any other document executed for the purpose of creating, securing or guarantying the Secured Debt;
- C. The making or furnishing of any verbal or written representation, statement or warranty to Lender that is false or incorrect in any material respect by Mortgagor or any person or entity obligated on the Secured Debt;
- D. The death, dissolution, or insolvency of, appointment of a receiver for, or application of any debtor relief law to, Mortgagor or any other person or entity obligated on the Secured Debt;
- E. Any loan proceeds are used for a purpose that will contribute to excessive erosion of highly erodible land or to the conversion of wetlands to produce an agricultural commodity, as further explained in 7 C.F.R. Part 1940, Subpart G, Exhibit M.

17. REMEDIES ON DEFAULT. In some instances, federal and state law will require Lender to provide Mortgagor with notice of the right to cure or other notices and may establish time schedules for foreclosure actions. Subject to these limitations, if any, Lender may accelerate the Secured Debt and foreclose this Security Instrument in a manner provided by law if Mortgagor is in default.

At the option of Lender, all or any part of the agreed fees and charges, accrued interest and principal shall become immediately due and payable after giving notice if required by law upon the occurrence of a default or anytime thereafter. In addition, Lender shall be entitled to all of the remedies provided by law, the terms of the Secured Debt, this Security Instrument and any related documents. All remedies are distinct, cumulative and not exclusive, and Lender is entitled to all remedies provided at law or in equity whether or not expressly set forth. The acceptance by Lender of any sum in payment or partial payment on the Secured Debt after the balance is due or is accelerated or after foreclosure proceedings are filed shall not constitute a waiver of Lender's right to

require complete cure of any existing default. By not exercising any remedy on Mortgagor's default, Lender does not waive Lender's right to consider the event a default at a later time.

18. EXPENSES; ADVANCES ON COVENANTS; ATTORNEYS' FEES; COLLECTION COSTS. Except when prohibited by law, Mortgagor agrees to pay all of Lender's expenses if Mortgagor breaches any covenant in this Security Instrument. Mortgagor will also pay on demand any amount incurred by Lender for insuring, inspecting, preserving or otherwise protecting the Property and Lender's security interest. These expenses will bear interest from the date of the payment until paid in full at the highest interest rate in effect as provided in the terms of the Secured Debt. Mortgagor agrees to pay all costs and expenses incurred by Lender in collecting, enforcing or protecting Lender's rights and remedies under this Security Instrument. This amount may include, but is not limited to, attorneys' fees, court costs, and other legal expenses. This Security Instrument shall remain in effect until released. Mortgagor agrees to pay for any recordation costs of such release.

19. ENVIRONMENTAL LAWS AND HAZARDOUS SUBSTANCES. As used in this section, (1) Environmental Law means, without limitation, the Comprehensive Environmental Response, Compensation and Liability Act (CERCLA, 42 U.S.C. 9601 et seq.), all other federal, state and local laws, regulations, ordinances, court orders, attorney general opinions or interpretive letters concerning the public health, safety, welfare, environment or a hazardous substance; and (2) Hazardous Substance means any toxic, radioactive or hazardous material, waste, pollutant or contaminant which has characteristics which render the substance dangerous or potentially dangerous to the public health, safety, welfare or environment. The term includes, without limitation, any substances defined as "hazardous material," "toxic substances," "hazardous waste," "hazardous substance," or "regulated substance" under any Environmental Law.

Mortgagor represents, warrants and agrees that:

- A. Except as previously disclosed and acknowledged in writing to Lender, no Hazardous Substance has been, is, or will be located, transported, manufactured, treated, refined, or handled by any person on, under or about the Property, except in the ordinary course of business and in strict compliance with all applicable Environmental Law.
- B. Except as previously disclosed and acknowledged in writing to Lender, Mortgagor has not and will not cause, contribute to, or permit the release of any Hazardous Substance on the Property.
- C. Mortgagor will immediately notify Lender if (1) a release or threatened release of Hazardous Substance occurs on, under or about the Property or migrates or threatens to migrate from nearby property; or (2) there is a violation of any Environmental Law concerning the Property. In such an event, Mortgagor will take all necessary remedial action in accordance with Environmental Law.
- D. Except as previously disclosed and acknowledged in writing to Lender, Mortgagor has no knowledge of, or reason to believe there is, any pending or threatened investigation, claim, or proceeding of any kind relating to (1) any Hazardous Substance located on, under or about the Property; or (2) any

violation by Mortgagor or any tenant of any Environmental Law. Mortgagor will immediately notify Lender in writing as soon as Mortgagor has reason to believe there is any such pending or threatened investigation, claim, or proceeding. In such an event, Lender has the right, but not the obligation, to participate in any such proceeding, including the right to receive copies of any documents relating to such proceedings.

- E. Except as previously disclosed and acknowledged in writing to Lender, Mortgagor and every tenant have been, are and shall remain in full compliance with any applicable Environmental Law.
- F. Except as previously disclosed and acknowledged in writing to Lender, there are no underground storage tanks, private dumps or open wells located on or under the Property and no such tank, dump or well will be added unless Lender first consents in writing.
- G. Mortgagor will regularly inspect the Property, monitor the activities and operations on the Property, and confirm that all permits, licenses or approvals required by any applicable Environmental Law are obtained and complied with.
- H. Mortgagor will permit, or cause any tenant to permit, Lender or Lender's agent to enter and inspect the Property and review all records at any reasonable time to determine (1) the existence, location and nature of any Hazardous Substance on, under or about the Property; (2) the existence, location, nature, and magnitude of any Hazardous Substance that has been released on, under or about the Property; or (3) whether or not Mortgagor and any tenant are in compliance with applicable Environmental Law.
- I. Upon Lender's request and at any time, Mortgagor agrees, at Mortgagor's expense, to engage a qualified environmental engineer to prepare an environmental audit of the Property and to submit the results of such audit to Lender. The choice of the environmental engineer who will perform such audit is subject to Lender's approval.
- J. Lender has the right, but not the obligation, to perform any of Mortgagor's obligations under this section at Mortgagor's expense.
- K. As a consequence of any breach of any representation, warranty or promise made in this section, (1) Mortgagor will indemnify and hold Lender and Lender's successors or assigns harmless from and against all losses, claims, demands, liabilities, damages, cleanup, response and remediation, costs, penalties and expenses, including without limitation all costs of litigation and attorneys' fees, which Lender and Lender's successors or assigns may sustain; (2) at Lender's discretion, Lender may release this Security Instrument and in return Mortgagor will provide Lender with collateral of at least equal value to the Property secured by this Security Instrument without prejudice to any of Lender's rights under this Security Instrument; and/or (3) at Lender's option, Lender may elect not to foreclose this Security Instrument, but instead,

Lender may bring an independent action or lawsuit to enforce the indemnification provisions regarding Hazardous Substances against Mortgagor. If Lender elects to seek the remedies provided for in item (3) above, Lender shall be entitled to all legal and equitable remedies, including, without limitation, those relating to damages for breach of contract, and Mortgagor acknowledges that, notwithstanding any other provision of this Security Instrument to the contrary, the obligation of Mortgagor under this Security Instrument are unlimited personal obligations of Mortgagor. No action for the enforcement of or recovery of damages under this Security Instrument shall constitute a deficiency judgment within the meaning of any anti-deficiency or one-action laws. Mortgagor acknowledges that Lender is unwilling to accept any consequences resulting from any violation of Environmental Law and that Lender would not make the loan but for the personal unsecured liability undertaken by Mortgagor as provided herein. The rights of Lender herein shall be cumulative and in addition to any other rights and remedies of Lender under any other document or instrument or at law or in equity.

L. Notwithstanding any of the language contained in this Security Instrument to the contrary, the terms of this section shall survive any foreclosure or satisfaction of this Security Instrument regardless of any passage of title to Lender or any disposition by Lender of any or all of the Property. Any claims and defenses to the contrary are hereby waived.

20. CONDEMNATION. Mortgagor will give Lender prompt notice of any pending or threatened action, by private or public entities to purchase or take any or all of the Property through condemnation, eminent domain, or any other means. Mortgagor authorizes Lender to intervene in Mortgagor's name in any of the above described actions or claims. Mortgagor assigns to Lender the proceeds of any award or claim for damages connected with a condemnation or other taking of all or any part of the Property. Such proceeds shall be considered payments and will be applied as provided in this Security Instrument. This assignment of proceeds is subject to the terms of any prior mortgage, deed of trust, security agreement or other lien document.

21. INSURANCE. Mortgagor agrees to maintain insurance as follows:

A. Mortgagor shall keep the Property insured against loss by fire, flood, theft and other hazards and risks reasonably associated with the Property due to its type and location. This insurance shall be maintained in the amounts and for the periods that Lender requires. The insurance carrier providing the insurance shall be chosen by Mortgagor subject to Lender's approval, which shall not be unreasonably withheld. If Mortgagor fails to maintain the coverage described above, Lender may, at Lender's option, obtain coverage to protect Lender's rights in the Property according to the terms of this Security Instrument.

All insurance policies and renewals shall be acceptable to Lender and shall include a standard "mortgage clause" and, where applicable, "loss payee clause." Mortgagor shall immediately notify Lender of cancellation or termination of the insurance. Lender shall have the right to hold the policies

and renewals. If Lender requires, Mortgagor shall immediately give to Lender all receipts of paid premiums and renewal notices. Upon loss, Mortgagor shall give immediate notice to the insurance carrier and Lender. Lender may make proof of loss not made immediately by Mortgagor.

Unless otherwise agreed in writing, all insurance proceeds shall be applied to restoration or repair of the Property or to the Secured Debt, whether or not then due, at Lender's option. Any application of proceeds to principal shall not extend or postpone the due date of scheduled payment nor change the amount of any payment. Any excess will be paid to the Mortgagor. If the property is acquired by Lender, Mortgagor's right to any insurance policies and proceeds resulting from damage to the Property before the acquisition shall pass to Lender to the extent of the Secured Debt immediately before the acquisition.

- B. Mortgagor agrees to maintain comprehensive general liability insurance naming Lender as an additional insured in an amount acceptable to Lender, insuring against claims arising from any accident or occurrence in or on the Property.
- C. Mortgagor agrees to maintain rental loss or business interruption insurance, as required by Lender, in an amount equal to at least coverage of one year's debt service, and required escrow account deposits (if agreed to separately in writing), under a form of policy acceptable to Lender.

22. ESCROW FOR TAXES AND INSURANCE. Unless otherwise provided in a separate agreement, Mortgagor will not be required to pay to Lender funds for taxes and insurance in escrow.

23. FINANCIAL REPORTS AND ADDITIONAL DOCUMENTS. Mortgagor will provide to Lender upon request, any financial statement or information Lender may deem reasonably necessary. Mortgagor agrees to sign, deliver, and file any additional documents or certifications that Lender may consider necessary to perfect, continue, and preserve Mortgagor's obligations under this Security Instrument and Lender's lien status on the Property.

24. JOINT AND INDIVIDUAL LIABILITY; CO-SIGNERS; SUCCESSORS AND ASSIGNS BOUND. All duties under this Security Instrument are joint and individual. If Mortgagor signs this Security Instrument but does not sign an evidence of debt, Mortgagor does so only to mortgage Mortgagor's interest in the Property to secure payment of the Secured Debt and Mortgagor does not agree to be personally liable on the Secured Debt. If this Security Instrument secures a guaranty between Lender and Mortgagor, Mortgagor agrees to waive any rights that may prevent Lender from bringing any action or claim against Mortgagor or any party indebted under the obligation. These rights may include, but are not limited to, any anti-deficiency or one-action laws. Mortgagor agrees that Lender and any party to this Security Instrument may extend, modify or make any change in the terms of this Security Instrument or any evidence of debt without Mortgagor's consent. Such a change will not release Mortgagor from the terms of this Security Instrument. The duties and benefit of this Security Instrument shall bind and benefit the successors and assigns of Mortgagor and Lender.

25. APPLICABLE LAW, SEVERABILITY, INTERPRETATION. This Security Instrument is governed by the laws of the jurisdiction in which Lender is located, except to the extent otherwise required by the laws of the jurisdiction where the Property is located. This Security Instrument is complete and fully integrated. This Security Instrument may not be amended or modified by oral agreement. Any section in this Security Instrument, attachments, or any agreement related to the Secured Debt that conflicts with applicable law will not be effective, unless that law expressly or impliedly permits the variations by written agreement. If any section of this Security Instrument cannot be enforced according to its terms, that section will be severed and will not affect the enforceability of the remainder of this Security Instrument. Whenever used, the singular shall include the plural and the plural the singular. The captions and headings of the sections of this Security Instrument are for convenience only and are not to be used to interpret or define the terms of this Security Instrument. Time is of the essence in this Security Instrument.

26. NOTICE. Unless otherwise required by law, any notice shall be given by delivering it or by mailing it by first class mail to the appropriate party's address on page 1 of this Security Instrument, or to any other address designated in writing. Notice to one mortgagor will be deemed to be notice to all mortgagors.

27. WAIVERS. Except to the extent prohibited by law, Mortgagor waives and releases any and all rights and remedies that Mortgagor may now have or acquire in the future relating to redemption, reinstatement, and the marshalling of liens and assets. Mortgagor waives all rights of valuation and appraisal.

28. U.C.C. PROVISIONS. If checked, the following are applicable to, but do not limit, this Security Instrument:

- ☐ CONSTRUCTION LOAN. This Security Instrument secures an obligation incurred for the construction of an improvement on the Property.
- ☒ FIXTURE FILING. Mortgagor grants to Lender a security interest in all goods that Mortgagor owns now or in the future and that are or will become fixtures related to the Property.
- ☐ CROPS; TIMBER, MINERALS; RENTS, ISSUES, AND PROFITS. Mortgagor grants to Lender a security interest in all crops, timber and minerals located on the Property as well as all rents, issues, and profits of them including, but not limited to, all Conservation Reserve Program (CRP) and Payment in Kind (PIK) payments and similar governmental programs (all of which shall also be included in the term "Property"). Lender may file a financing statement signed by Lender instead of Mortgagor with appropriate public officials.
- ☒ PERSONAL PROPERTY. Mortgagor grants to Lender a security interest in all personal property located on or connected with the Property, including all farm products, inventory, equipment, accounts, documents, instruments, chattel paper, general intangibles, and all other items of personal property that Mortgagor owns now or in the future and that are used or useful in the construction, ownership, operation, management, or maintenance of the Property (all of which shall also be included in the term "Property"). The term "personal property" specifically excludes that property described as "household goods" secured in connection with a "consumer"

loan as those terms are defined in applicable federal regulations governing unfair and deceptive credit practices. Lender may file a financing statement signed by Lender instead of Mortgagor with appropriate public officials.

☒ FILING AS FINANCING STATEMENT. Mortgagor agrees and acknowledges that this Security Instrument also suffices as a financing statement and any carbon, photographic or other reproduction may be filed of record for purposes of Article 9 of the Uniform Commercial Code.

29. OTHER TERMS. If checked, the following are applicable to this Security Instrument:

☐ LINE OF CREDIT. Secured Debt includes a revolving line of credit provision. Although the Secured Debt may be reduced to a zero balance, this Security Instrument will remain in effect until released.

☐ ADDITIONAL TERMS.

SIGNATURES: By signing below, Mortgagor agrees to the terms and covenants contained in this Security Instrument and in any attachments. Mortgagor also acknowledges receipt of a copy of this Security Instrument on the date stated on page 1.

Entity Name: Houba, Inc. Entity Name: _____

By: /s/ Michael Reicher 3/29/00 _____

Its: Chief Executive Officer

(Signature) _____ (Date) _____ (Signature) _____ (Date) _____

(Signature) _____ (Date) _____ (Signature) _____ (Date) _____

ACKNOWLEDGMENT:

STATE OF _____, COUNTY OF _____) ss.
(Individual) Before me, _____, a Notary Public this _____
day of _____, _____ acknowledged the
execution of the annexed mortgage.

My commission expires:

(Seal) (Notary Public) _____

(Notary's County) _____

STATE OF _____, COUNTY OF _____) ss.
Before me, _____, a Notary Public this _____ day of _____
_____(Titles)
of _____(Name of Business Entity)
a _____ acknowledged the execution of the annexed
mortgage of the business or entity.

My commission expires:

(Seal) (Notary Public)_____

(Notary's County)_____

This instrument was prepared by _____

LEGAL DESCRIPTION

EXHIBIT A

A part of the Northwest Quarter of Section 9, Township 32 North, Range 1 East, Union Township, Marshall County, Indiana, described as follows:

PARCEL "A"

Commencing at the Northeast corner of said Northwest Quarters thence South 0 degrees00'06" West along the East line of said Northwest Quarter a distance of 691.20 feet (691.30 feet record) to the point of beginning; thence South 89 degrees08'35" West a distance of 1313.44 feet to the West line of the East half of said Northwest Quarter thence South 1 degrees09'25" East along said West line a distance of 1011.80 feet thence South 89 degrees39'37" East a distance of 334.41 feet thence North 0 degrees00'00" East a distance of 307.73 feet thence North 90 degrees 00'00" East a distance of 428.47 feet thence North 0 degrees00'00" East a distance of 110.00 feet thence North 90 degrees 00'00" East a distance of 80.00 feet; thence North 0 degrees 00'00" East a distance 55.00 feet; thence North 90 degrees 00'00" East a distance of 50.00 feet thence North 0 degrees 00'00" East a distance of 10.00 feet; thence North 90 degrees 00'00" East a distance 208.00 feet to the East line of said Northwest Quarter; thence North 0 degrees00'00" East along said North line a distance of 531.88 feet to the point of beginning containing 24.077 acres more or less.

Subject to legal highways and segments of record.

The address of such real estate is commonly known as 16235 State Road 17, Culver, Indiana 46511.

PARCEL "B"

A part of the Northwest Quarter (NW 1/4) of Section 9, Township 32 North, Range 1 East, Union Township, Marshall County, Indiana, described as follows:

Commencing at the Northeast corner of said Northwest Quarter (NW 1/4); thence South 0 degrees00'00" West along the East line of said Northwest Quarter (NW 1/4) a distance of 1382.37 feet to the point of beginning; thence South 89 degrees52'41" West a distance of 200.00 feet; thence South 0 degrees00'00" West a distance of 346.00 feet; thence North 89 degrees39'37" West a distance of 558.48 feet; thence North 0 degrees00'00" East a distance of 307.73 feet; thence North 90 degrees00'00" East a distance of 428.47 feet; thence North 0 degrees00'00" East a distance of 110.00 feet; thence North 90 degrees00'00" East a distance of 80.00 feet; thence North 0 degrees00'00" East a distance of 55.00 feet; thence North 90 degrees00'00" East a distance of 50.00 feet; thence North 0 degrees00'00" East a distance of 10.00 feet; thence North 90 degrees00'00" East a distance of 200.00 feet to said East line; thence South 0 degrees00'00" West along said East line a distance of 139.62 feet to the point of beginning, containing 5.00 acres, more or less.

The address of such real estate is commonly known as 16235 State Road 17, Culver, Indiana 46511.

EXHIBIT B

Loan Agreement dated March 29, 2000, by and between Lender and Mortgagor pursuant to which Lender agreed to lend, and Mortgagor agreed to borrow, the principal amount of Seventeen Million Five Hundred Thousand Dollars (\$17,500,000.00).

STATE OF INDIANA _____ SPACE ABOVE THIS LINE FOR
RECORDING DATA

SUBORDINATION AGREEMENT

(MORTGAGES TO MORTGAGE)

NOTICE: THIS SUBORDINATION AGREEMENT RESULTS IN YOUR SECURITY
INTEREST IN THE PROPERTY BECOMING SUBJECT TO AND OF
LOWER PRIORITY THAN THE LIEN OF PRIMARY
LENDER'S MORTGAGE (DEFINED BELOW)

This SUBORDINATION AGREEMENT (the "Agreement") is made as of March 29, 2000 by and among HOUBA, an Indiana corporation, the owner of the real property hereinafter described ("Owner"), GALEN PARTNERS, III, L.P., a Delaware limited partnership ("Galen") and ORACLE STRATEGIC PARTNERS, L.P., a Delaware limited partnership ("Oracle") holders of the mortgages described below (collectively, "Subordinate Lenders"), in favor of WATSON PHARMACEUTICALS, INC., a Nevada corporation ("Primary Lender").

R E C I T A L S

- A. Owner has executed, or proposes to execute, a Real Estate Mortgage (With Future Advance Clause) ("Primary Lender's Mortgage") securing, among other things, repayment of a promissory note ("Note") in the principal amount of Seventeen Million Five Hundred Thousand Dollars (\$17,500,000), dated as of March 29, 2000 in favor of Primary Lender (the "Primary Loan"), pursuant to which Owner grants to Primary Lender a security interest in and to the property described on Exhibit A attached hereto and made a part hereof (which property, together with all improvements now or hereafter located on the property, is hereinafter referred to as the "Property"). Primary Lender's Mortgage is to be recorded prior to this Agreement.
- B. Pursuant to the terms and provisions of (i) that certain mortgage dated March 10, 1998 and recorded April 14, 1998 as Mortgage Record 9803137 in the official records of Marshall County, Indiana (the "Official Records") securing repayment of a promissory note in the principal amount of Twenty Million Eight Hundred Thousand Dollars (\$20,800,000) executed by Owner in favor of Galen and (ii) that certain mortgage dated May 26, 1999 and recorded June 28, 1999 as Mortgage Record 9905386 in the Official Records in the principal amount of Twenty-Two Million Eight Hundred Sixty-Three Thousand Dollars (\$22,863,000) executed by Owner in favor of Oracle, Owner granted to Subordinate Lenders a security interest in and to the Property.
- C. As a condition of the Primary Lender making the Primary Loan secured by Primary Lender's Mortgage, Primary Lender requires that Primary Lender's Mortgage be unconditionally and at all times remain a lien or charge upon the Property, prior and superior to all the rights of Subordinate Lenders under their mortgages with respect to the Primary Loan outstanding at any time, accrued and unpaid interest thereon and reasonable costs and expenses of enforcement by Watson of its rights and collection with respect to the Primary Loan (the "Senior Debt"), and that the Subordinate Lenders specifically and unconditionally subordinate their mortgages to the lien or charge of Primary Lender's Mortgage with respect to the Senior Debt.
- D. The Subordinate Lenders and Owner agree to the foregoing subordination in favor of Primary Lender.

NOW, THEREFORE, for valuable consideration and to induce Primary Lender to make the Primary Loan, Owner and the Subordinate Lenders hereby agree for the benefit of Primary Lender as follows:

- 4.1 The foregoing recitals are incorporated herein by this reference. Primary Lender's Mortgage, the Note in favor of Primary Lender, and shall unconditionally be and at all times remain a lien or charge on the Property to the extent they secure the Senior Debt prior and superior to the mortgages of the Subordinate Lenders; and
- 4.2 This Agreement shall be the whole agreement with regard to the subordination of the mortgages of the Subordinate Lenders to the lien or charge of Primary Lender's Mortgage, and shall supersede and cancel, but only insofar as would affect the priority of Primary Lender's Mortgage to the extent securing the Senior Debt, any prior agreements as to such subordination, including, without limitation, those provisions, if any, contained in the mortgages of the Subordinate Lenders which provide for the subordination of the mortgage of any later or subsequent lender to a deed or to a mortgage or mortgages.

Subordinate Lenders further declare, agree and acknowledge for the benefit of Primary Lender, that:

- 4.3 Primary Lender, in making disbursements pursuant to any such agreement, is under no obligation or duty to, nor has Primary Lender represented that it will, see to the application of such proceeds by the person or persons to whom Primary Lender disburses such proceeds, and any application or use of such proceeds for purposes other than those provided for in such agreement or agreements shall not defeat the subordination herein made in whole or in part; and
- 4.4 Subordinate Lenders intentionally and unconditionally subordinate all of Subordinate Lenders' rights, title and interest in and to the Property to the lien or charge of Primary Lender's Mortgage to the extent securing the Senior Debt upon the Property and understand that in reliance upon, and in consideration of, this subordination, specific loans and advances are being and will be made by Primary Lender and, as part and parcel thereof, specific monetary and other obligations are being and will be entered into which would not be made or entered into but for the reliance upon this subordination.

- 5. This Agreement may be executed in two or more counterparts, each of which shall be deemed an original and all of which together shall constitute and be construed as one and the same instrument.

NOTICE: THIS SUBORDINATION AGREEMENT CONTAINS A PROVISION WHICH MAY ALLOW THE PERSON OBLIGATED ON YOUR REAL PROPERTY SECURITY TO OBTAIN A LOAN, A PORTION OF WHICH MAY BE EXPENDED FOR PURPOSES OTHER THAN IMPROVEMENT OF THE PROPERTY.

IT IS RECOMMENDED THAT, PRIOR TO THE EXECUTION OF THIS AGREEMENT, THE PARTIES CONSULT WITH THEIR ATTORNEYS WITH RESPECT THERETO.

"Owner"

HOUBA, INC.,
an Indiana corporation

By: /s/ Michael Reicher
Name:

Chief Executive Officer

"Subordinate Lenders"

ORACLE STRATEGIC PARTNERS, L.P.,
a Delaware limited partnership

By: Oracle Strategic Capital. L.L.C.,
General Partner
712 Fifth Avenue
New York, New York 10019

Name: /s/ Larry Feinberg

Title: Managing Member

GALEN PARTNERS III, L.P.
a Delaware limited partnership

By: Claudius, L.L.C.,
General Partner
610 Fifth Avenue, Fifth Floor
New York, New York 10019

Name: /s/ Bruce F. Wesson

Title: Senior Managing Member

(ALL SIGNATURES MUST BE ACKNOWLEDGED)

PRODUCT PURCHASE AGREEMENT
[(_____)]

This Product Purchase Agreement (the "Agreement") is dated as of March 29, 2000, between Watson Pharmaceuticals, Inc., a Nevada corporation, ("Watson") and Halsey Drug Co., Inc., a New York corporation, ("Halsey").

RECITALS

1. Halsey exclusively owns the Product Assets (as defined below).
2. Watson desires to acquire, and Halsey is willing to transfer, the Product Assets as provided herein.
3. Halsey desires to manufacture for Watson the Product (as defined below) and [_____] active ingredient and Watson desires to purchase such materials from Halsey.
4. To facilitate the completion of certain facility improvements to enable Halsey to supply Product and [_____] to Watson and for other general corporate purposes, including, without limitation, working capital, Halsey desires to borrow from Watson \$17,500,000 pursuant to a secured Note and Watson desires to loan such amount to Halsey.
5. Halsey has or may acquire, rights to manufacture other pharmaceutical compounds and desire to provide Watson the opportunity to negotiate supply arrangements for such other compounds.
6. In consideration of the foregoing premises and of the mutual covenants and obligations set forth herein, the parties hereto agree as follows:

ARTICLE 1

DEFINITIONS

- 1.1 "AFFILIATES" shall mean, with respect to any party, any person or entity which, directly or indirectly through one or more intermediaries, controls, is controlled by, or is under common control with, such party. A person or entity shall be deemed to control a corporation (or other entity) if such person or entity possesses, directly or indirectly, the power to direct or cause the direction of the management and policies of such corporation (or other entity) whether through the ownership of voting securities, by contract or otherwise.
- 1.2 "ANDA" shall mean an Abbreviated New Drug Application filed with the FDA.
- 1.3 "API" shall mean the active pharmaceutical ingredient [_____].
- 1.4 "ASSIGNED CONTRACTS" shall mean those contracts set forth in the Disclosure Letter.

1.5 "DISCLOSURE LETTER" shall mean that certain Disclosure Letter dated the date hereof from Halsey to Watson.

1.6 "DRUG MASTER FILE" shall mean Halsey's Drug Master File for manufacturing the API, filed with the FDA, and the equivalent filing with the governing health authority of any other country, as same may be amended from time to time.

1.7 "EXCLUSIVE INTELLECTUAL PROPERTY" shall mean Intellectual Property exclusively relating to the research, development, manufacture, use and registration of the Product throughout the world, including, without limitation, the Intellectual Property as set forth in the Disclosure Letter.

1.8 "FDA" shall mean the United States Food and Drug Administration, and any successor agency thereto.

1.9 "INTELLECTUAL PROPERTY" shall mean all of Halsey's and its Affiliates' rights, existing as of the date hereof or as may be developed or acquired hereafter through the date that Watson receives notice from the FDA that the ANDA for the Product has been approved as set forth in Section 3.1.1 below, in and to all confidential or proprietary information, trade secrets, trade names, trademarks, copyrights, patent rights, research and results thereof, technology, know-how, discoveries, records of inventions (whether or not patentable), developments, improvements, techniques, data, methods, processes, instructions, formulae, recipes, drawings and specifications relating to the research, development, manufacture, use and registration of the Product and the API throughout the world, including without limitation, such information and data relating to specifications for materials and equipment necessary for manufacture, methods of production and formulation, the chemical and physical properties, preclinical and clinical studies, including safety and efficacy data, and procedures of testing and validation and requirements of quality control; provided, however, that notwithstanding the foregoing, Intellectual Property shall not include the Drug Master File.

1.9 "LICENSED INTELLECTUAL PROPERTY" shall mean Intellectual Property which is not Exclusive Intellectual Property.

1.10 "OTHER PRODUCT ASSETS" shall mean those other tangible and intangible assets related to the Product as set forth in the Disclosure Letter.

1.11 "PRODUCT" shall mean all formulations of [_____] in capsule, tablet or other form for oral administration, including without limitation the formulation described in the Product ANDA.

1.12 "PRODUCT ASSETS" shall mean the Exclusive Intellectual Property, the Regulatory Dossiers, the Assigned Contracts and the Other Product Assets.

1.13 "PRODUCT ANDA" shall mean the ANDA No. [_____] for formulations of [_____] for oral administration.

1.14 "REGULATORY DOSSIERS" shall mean all registrations, permits, licenses, authorizations, approvals, presentations, notifications or filings (together with all applications therefor), which are

filed with or granted by the FDA or other governing health authority of any country, and which are required to develop, make, use, sell, import or export the Product or the API, including without limitation, the Product ANDA and those set forth in the Disclosure Letter, and any supporting data, studies or documents thereto; provided, however, that notwithstanding the foregoing Regulatory Dossiers shall not include the Drug Master File.

ARTICLE 2

TRANSFER OF PRODUCT ASSETS

2.1 TRANSFER OF PRODUCT ASSETS. Halsey, on behalf of itself and each of its Affiliates, does hereby sell, convey, transfer, assign and deliver to Watson all of Halsey's and its Affiliates' right, title and interest in and to the Product Assets throughout the world, free and clear of all claims, liens, pledges, encumbrances, mortgages, taxes, and equities of any kind whatsoever. In order to further perfect and evidence Watson's interest in the Product Assets (including without limitation the Exclusive Intellectual Property), Halsey shall execute and deliver patent, trademark or other assignments or bills of sale or other documents as may be reasonably requested by Watson.

2.2 LICENSE OF LICENSED INTELLECTUAL PROPERTY. Halsey hereby grants to Watson a non-exclusive, perpetual, irrevocable, royalty-free license to use and practice the Licensed Intellectual Property for any and all purposes, including, without limitation, the research, development manufacture, use, registration, marketing, promotion, advertising or sale of the Product and the API throughout the world.

2.3 ASSIGNMENT OF CONTRACTS. Halsey, on behalf of itself, and for each of its Affiliates, does hereby assign to Watson all of Halsey's and its Affiliates' right, title and interest in and to the Assigned Contracts, free and clear of all claims, liens, pledges, encumbrances, mortgages, taxes and equities of any kind whatsoever. In order to further protect and evidence Watson's interest in the Assigned Contracts, Halsey shall execute and deliver any additional assignments or documents as may be reasonably requested by Watson.

2.4 DELIVERY OF KNOW-HOW. After execution of this Agreement, Halsey shall promptly furnish to Watson copies of documents in the possession or control of Halsey or its Affiliates that embody the Intellectual Property and that are reasonably necessary or useful to enable Watson to utilize and commercially exploit, the Intellectual Property. Halsey shall make available its personnel to facilitate the transfer of the Intellectual Property and to enable Watson to utilize the Intellectual Property.

2.5 DELIVERY OF REGULATORY DOSSIERS. After execution of this Agreement, Halsey shall promptly furnish to Watson originals of all Regulatory Dossiers, and all files, records and data (including all those in electronic or digital form) related thereto or necessary in the preparation or production thereof, in the possession or control of Halsey or its Affiliates that relate to the Product and/or the API. At Watson's request, Halsey shall provide to the FDA or other regulatory agencies any assignments, consents or other documents necessary to transfer the ownership of the Regulatory Dossiers to Watson.

2.6 OTHER PRODUCT ASSETS. After execution of this Agreement, Halsey shall promptly deliver to the possession of Watson the Other Product Assets.

2.7 ASSIGNMENT, LICENSE, SUBLICENSE. Watson may sell, assign, transfer, license, sublicense or otherwise convey to any person or entity all or part of the rights (but not its obligations) granted to Watson under this Article 2 without Halsey's consent. Watson's obligations under this Agreement shall not be reduced by virtue of any such transfer, and Watson shall be primarily liable for all of its obligations hereunder, including, without limitation, the payment obligations provided in Section 3.1.

2.8 FURTHER ASSURANCES. Halsey shall, and shall cause its Affiliates to, execute and deliver all other documents and instruments of conveyance, transfer or assignment and take all other actions reasonably requested by Watson to effect the sale and transfer to Watson of the Product Assets in accordance with this Agreement.

ARTICLE 3

PAYMENTS, OTHER AGREEMENTS

3.1 PURCHASE PRICE. As consideration for the license of the Licensed Intellectual Property and the assignment of the Exclusive Intellectual Property, Regulatory Dossiers, the Assigned Contracts and Other Product Assets and the other obligations of Halsey, Watson shall pay to Halsey, up to an aggregate of Thirteen Million Five Hundred Thousand Dollars (\$13,500,000) as follows:

3.1.1 [] within thirty (30) days after Watson receives [] is obtained by December 31, 2000.

3.1.2 [] within thirty (30) days after Halsey receives []

[], provided such conditions are met by May 1, 2001. []

[]

3.1.3 [] within ten (10) days after Watson receives [] of the API for the Product and all of Watson's currently marketed pharmaceutical products containing the API (as set forth in the letter to Halsey dated the date hereof) and any modifications thereof that would be subject to a supplement or annual report, provided such FDA notice is received by July 1, 2001.

3.1.4 In the event the conditions set forth in Section 3.1.1 are not met, the obligation of Watson to make payments under Sections 3.1.2 and 3.1.3 shall terminate. In addition, in the event the conditions set forth in Sections 3.1.1, 3.1.2 and 3.1.3 are not met by the respective

dates set forth therein, the obligation of Watson to make such corresponding payments shall terminate

3.2 SUPPLY AGREEMENTS. Concurrently herewith, Watson and Halsey shall enter into a Finished Goods Supply Agreement in the form of Exhibit A hereto and a Active Ingredient Supply Agreement in the form of Exhibit B hereto.

3.3 LOAN. Concurrently herewith, Watson is loaning Seventeen Million Five Hundred Thousand Dollars (\$17,500,000) pursuant to a Loan Agreement of even date herewith.

3.4 LEGAL OPINION. Concurrently herewith, Watson shall receive an opinion of St. John & Wayne, L.L.C., counsel to Halsey, dated as of the date hereof in the form of Exhibit C hereto.

ARTICLE 4

DEVELOPMENT

4.1 REGULATORY MATTERS. Pursuant to Section 2.1, upon execution of this Agreement, the ownership of the Product ANDA shall be transferred to Watson. Halsey shall be responsible for, and shall have the right to conduct, subject to this Agreement, the prosecution of the Product ANDA in the name of Watson and agrees to use commercially reasonable efforts and diligence to obtain FDA approval of the Product ANDA in accordance with its business, legal, medical and scientific judgment, such commercially reasonable efforts to be in accordance with the efforts and resources Halsey would use for a product owned by it or to which it has rights, which is of similar market potential at a similar stage in its product life, taking into account the competitiveness of the marketplace, the proprietary position of the Product, the regulatory structure involved, the profitability of the Product and other relevant factors. Each party shall pay their own expenses in connection with the FDA approval of the Product ANDA.

4.2 CONSULTATION. In carrying out the registration of the Product, Halsey shall consult with Watson and Watson shall cooperate and provide, at no fee or other charge, such services as Halsey reasonably requests. Halsey shall promptly provide to Watson copies of all correspondence received from, and written summaries of telephone conversations with, the FDA relating to the prosecution of the Product ANDA. No filings with or correspondence to the FDA shall be made by Halsey in the absence of obtaining Watson's written consent to such filings or correspondence, which consent shall not be unreasonably withheld or delayed. Halsey shall give Watson reasonable advance notice of any meetings or telephone conferences with representatives of the FDA relating to the prosecution of the Product ANDA in order to allow Watson an opportunity to attend any such meeting or participate in any telephone conference with the FDA. In prosecuting the Product ANDA and communicating with the FDA, the parties shall operate on a consensual basis. Any nonconcurrence between the parties shall be elevated to the Chief Operating Officer or his designee of each of the respective parties for resolution. In the event of any continuing nonconcurrence, the decision of the President or Chief Operating Officer of Watson shall be final and controlling.

4.3 COOPERATION. Halsey shall, upon request and at the expense of Watson, cooperate with Watson in connection with any matter pertaining to the protection of the Exclusive Intellectual Property whether in the courts, administrative or quasi-judicial agencies, or otherwise.

4.4 OBLIGATIONS RELATING TO API. Halsey agrees to use commercially reasonable efforts and diligence to obtain FDA approval to relocate its manufacturing site as described in Section 3.1.2 above and to assist Watson in obtaining FDA approval of Halsey as an approved source of the API as described in Section 3.1.3 above, in accordance with the standard provided in Section 4.1 above. Watson agrees to use commercially reasonable efforts and diligence to obtain FDA approval of Halsey as an approved source of the API, in accordance with the standard provided in Section 4.1 above, including, without limitation, the timely preparation and submission of stability studies and such other information and data as may be required or otherwise requested by the FDA.

ARTICLE 5

REPRESENTATIONS, WARRANTIES AND COVENANTS

5.1 HALSEY REPRESENTATIONS AND WARRANTIES. Halsey represents and warrants as of the date hereof, and, with respect to Sections 5.1.7 and 5.1.8, on each date that Halsey is entitled to payment hereunder, as follows:

5.1.1 CORPORATE AUTHORITY. Halsey is a corporation duly organized, validly existing and in good standing under the laws of the State of New York. Halsey has the power and authority to own and transfer the Product Assets as provided herein. Halsey has the power and authority to execute and deliver this Agreement, any the instruments to be executed and delivered by it pursuant hereto and to consummate the transactions contemplated hereby. All acts required to be taken by or on the part of Halsey (corporate or otherwise) to authorize the execution, delivery and performance of this Agreement have been duly and properly taken and this Agreement has been duly and promptly executed and delivered by Halsey and constitutes a legal, valid and binding obligation of Halsey, except as enforcement may be limited by applicable bankruptcy, insolvency, reorganization and moratorium laws and other laws of general application affecting enforcement of creditors' rights generally.

5.1.2 OWNERSHIP, TITLE. Halsey is the sole and exclusive owner of the entire right, title and interest in and to each of the Product Assets throughout the world and has the right to transfer and assign each of the Product Assets to Watson under this Agreement. Halsey has good and marketable title to each of the Product Assets, subject to the receipt of executed copies of the UCC-3 Termination Statements attached as Exhibit E and the filing of same in the jurisdictions indicated thereon, free from any liens or encumbrances, and upon consummation of the transactions contemplated hereby, good and marketable title to each of the Product Assets shall be vested in Watson. All employees, consultants, advisors or contractors who have developed or assisted, in the development, or will develop or assist in the development, of the Intellectual Property, have executed valid assignments of their rights to Halsey and Halsey has supplied copies of all such assignments to Watson.

5.1.3 ASSIGNED CONTRACTS. Halsey has provided to Watson true and correct copies of each of the Assigned Contracts. Each of the Assigned Contracts is in full force and effect and no party to such Assigned Contracts is in breach thereof, nor is there any event or circumstance, which with the passage of time or the giving of notice, would give rise to any breach thereof. Halsey has not received any notice, nor does it have reason to believe, that any party to the Assigned Contracts intends to terminate or modify such Assigned Contracts.

5.1.4 NO CONFLICT. The execution, delivery and performance of this Agreement by Halsey will not result in the creation of any lien or encumbrance on any of the Product Assets, or violate, conflict with or result in a breach of or constitute a default (or an event with which the giving of notice, lapse of time or both, would become a default), under any order or decree of any court, administrative agency or governmental authority, the charter documents of Halsey or any agreement, contract (including, without limitation, the Assigned Contracts) or any other instrument to which Halsey or any other Affiliate is a party or to which its or their assets or property may be bound or affected. Except (i) as contemplated herein, (ii) as contemplated by the UCC-3 Termination Statements attached as Exhibit D hereto, (iii) for the consent of Galen Partners III L.P., as Agent under that certain Debenture and Warrant Purchase Agreement dated March 10, 1998 between Halsey, Galen Partners III, L.P. and each of the other signatories thereto, and (iv) for the consent of Oracle Strategic Partners, L.P. pursuant to that certain Debenture and Warrant Purchase Agreement dated May 26, 1999 between Halsey, Oracle Strategic Partners, L.P. and the other signatories thereto (all of which have been obtained and provided to Watson), no approval, authorization, consent or other order or action of or filing with or providing notice to any court, administrative agency, governmental authority or any other third party is required for the execution, delivery or performance of Halsey under this Agreement.

5.1.5 LITIGATION. There is no pending, or to its knowledge threatened, litigation that would reasonably be expected to affect adversely its right and ability to perform its obligations under this Agreement or the right of Watson to utilize the Product Assets or the Licensed Intellectual Property.

5.1.6 INFRINGEMENT. There is no pending, or to its knowledge threatened, claim, and Halsey has no knowledge of any basis for any claim that the use of the Intellectual Property or the manufacture and sale of the Product or the API would infringe or violate any patent, trademark, trade name, service mark, copyright, trade secret or other intellectual property right owned or claimed by another person or entity.

5.1.7 PRODUCT FORMULATION. To Halsey's knowledge, there are no defects in design or formulation of the Product which would adversely affect performance or create an unusual risk of injury to persons or property.

5.1.8 REGULATORY MATTERS. To the best of Halsey's knowledge, all of the Regulatory Dossiers, and the Drug Master File are free of any misrepresentations or omissions on the part of Halsey, its Affiliates, predecessors-in-interest or agents, that all steps taken by Halsey, its Affiliates, predecessors-in-interest or agents in the collection, assembly and presentation of the data in such Regulatory Dossiers were legitimate and reasonable when viewed within the standards of the industry, and that all responses of Halsey, its Affiliates, predecessors-in-interest or agents on behalf of itself or on behalf of Watson to any inquiries of the FDA were made in good faith.

5.2 WATSON REPRESENTATIONS AND WARRANTIES. Watson represents and warrants as of the date hereof as follows:

5.2.1 CORPORATE AUTHORITY. Watson is a corporation duly organized, validly existing and in good standing under the laws of the State of Nevada. Watson has the power and authority to own and use the Product Assets as provided herein. Watson has the power and authority to execute and deliver this Agreement, any the instruments to be executed and delivered by it pursuant hereto and to consummate the transactions contemplated hereby. All acts required to be

taken by or on the part of Watson (corporate or otherwise) to authorize the execution, delivery and performance of this Agreement have been duly and properly taken and this Agreement has been duly and promptly executed and delivered by Watson and constitutes a legal, valid and binding obligation of Watson, except as enforcement may be limited by applicable bankruptcy, insolvency, reorganization and moratorium laws and other laws of general application affecting enforcement of creditors' rights generally.

5.2.2 NO CONFLICT. The execution, delivery and performance of this Agreement by Watson will not violate, conflict with or result in a breach of or constitute a default (or event with which the giving of notice, lapse of time or both, would become a default), under any order or decree of any court, administrative agency or governmental authority, the charter documents of Watson or any agreement, contract or any other instrument to which Watson or any other Affiliate is a party or to which its or their assets or property may be bound or affected. No approval, authorization, consent or other order or action of or filing with or providing notice to any court, administrative agency, governmental authority or any other third party is required for the execution, delivery or performance of Watson under this Agreement.

5.2.3 LITIGATION. There is no pending, or to its knowledge threatened, litigation that would reasonably be expected to affect adversely its right and ability to perform its obligations under this Agreement.

ARTICLE 6

CONFIDENTIALITY

6.1 PROTECTION OF CONFIDENTIAL INFORMATION. Watson and Halsey shall:

(a) not disclose any confidential and proprietary information of the other to third parties except to: (i) government authorities; or (ii) such party's Affiliates, consultants or actual or potential contract manufacturers, licensees, distributors, purchasers, joint ventures, clinical investigators or other persons having bona fide business relations with such party, in each case pursuant to a non-disclosure commitment; and

(b) take such precautions as it normally takes with its own confidential and proprietary information to prevent disclosure to third parties of any confidential and proprietary information (except as contemplated above).

6.2 EXCEPTIONS. No party shall be obligated to maintain confidentiality under this Article with respect to any information that:

(a) at the time of disclosure is or thereafter becomes available to the general public other than by breach of this Article by such party;

(b) is obtained by such party from a third-party source who is not breaching a commitment of confidentiality to the other party to this Agreement by disclosing such information to such first party; or

(c) is required to be disclosed pursuant to law to protect such party's interest or in connection with any litigation, investigation or regulatory proceeding, or as otherwise required by law.

ARTICLE 7

INDEMNITY

7.1 INDEMNITY OBLIGATIONS. Each party shall defend, indemnify and hold harmless the other party hereto and its Affiliates, successors and permitted assigns (and the respective officers, directors, stockholders, partners and employees of each) from and against any and all losses, liabilities, claims, actions, proceedings, damages and expenses arising out of any breach of this Agreement by such party.

7.2 INDEMNIFICATION. If a party intends to claim indemnification under this Article 7 (the "Indemnified Party"), it shall notify the party against whom indemnification is sought (the "Indemnifying Party") promptly in writing of any action, claim or liability in respect of which the Indemnified Party believes it is entitled to claim indemnification, provided that the failure to give such timely notice shall not release the Indemnifying Party from any liability to the Indemnified Party except to the extent the Indemnifying Party is prejudiced thereby. The Indemnifying Party shall have the right, by notice to the Indemnified Party, to assume the defense of any third party action or claim which may give rise to indemnification hereunder. If the Indemnifying Party so assumes such defense, the Indemnified Party may participate therein through counsel of its choice, but at the sole cost of the Indemnified Party.

7.3 RIGHT OF OFFSET. Watson shall have the right to set off and retain any amounts, otherwise payable to Halsey hereunder to satisfy any indemnification claim Watson may have hereunder.

7.4 EXCLUSION OF WARRANTIES. Except as expressly provided in this Agreement, neither party makes any representation or warranty to the other, whether expressed or implied, either in fact or by operation of law, by statute, or otherwise, and both parties specifically disclaim any and all implied or statutory warranties including, without limitation, any warranty of merchantability or warranty of fitness for a particular purpose.

7.5 DISCLAIMER. Neither party shall be liable to the other for any consequential, incidental or indirect damages or expenses, including damages for lost profits, loss of opportunity or use or any kind, suffered by the other party, whether in contract, tort or otherwise.

ARTICLE 8

MISCELLANEOUS

8.1 INDEPENDENT CONTRACTORS. This Agreement does not constitute Watson as the agent or legal representative of Halsey, nor does it constitute Halsey as the agent or legal representative of Watson. Neither Watson nor Halsey shall have any right or authority to assume or create any obligation or responsibility or vicarious liability, express or implied, on behalf of or in the name of the other, or to bind the other in any manner.

8.2 NOTICES. All notices or other communications given pursuant hereto by one party hereto to the other party shall be in writing and deemed given (a) when delivered by messenger, (b) when sent by telecopier, (with receipt confirmed), (c) when received by the addressee, if sent by Express Mail, Federal Express or other express delivery service (receipt requested), or (d) five days

after being mailed in the U.S., first-class postage prepaid, registered or certified, in each case to the appropriate addresses and telecopier numbers set forth below (or to such other addresses and telecopier numbers as a party may designate as to itself by notice to the other party):

If to Watson, to it at:

Watson Pharmaceuticals, Inc.
311 Bonnie Circle
Corona, CA 92880
Attention: General Counsel
Telecopier No.: (909) 279-8094

If to Halsey, to it at:

Halsey Drug Company, Inc.
695 N. Perryville Road
Rockford, Illinois 61107
Attention: Chief Executive Officer
Telecopier No.: (805) 399-9710

8.3 FORCE MAJEURE. Neither party shall be responsible or liable to the other hereunder for failure or delay in performance of this Agreement due to any war, fire, accident or other casualty, or any labor disturbance, or act of God or the public enemy, or governmental action or any other contingency beyond such party's reasonable control. In the event of the applicability of this Section, the party affected by such force majeure shall use reasonable efforts, consistent with good business judgment, to eliminate, cure and overcome any of such causes and resume performance of its obligations.

8.4 SUCCESSORS AND ASSIGNS. Halsey may not assign this Agreement or assign or delegate its duties hereunder without the prior written consent of Watson. All of the terms and provisions of this Agreement shall be binding upon and inure to the benefit of and be enforceable by the parties hereto and their respective successors and assigns.

8.5 AMENDMENT. This Agreement may be amended only by written agreement of the parties hereto.

8.6 WAIVER. The failure of a party to insist upon strict adherence to any term of this Agreement on any occasion shall not be considered a waiver of that or any other term hereof or deprive that party of the right thereafter to insist upon strict adherence to that term or any other term of this Agreement. Any waiver must be in writing and be signed by the party against whom the waiver is asserted.

8.7 FURTHER ACTIONS. Each party agrees to execute, acknowledge and deliver such further instruments, and to do all such other acts, as may be reasonably necessary or appropriate in order to carry out the purpose and intent of this Agreement.

8.8 GOVERNING LAW, DISPUTE RESOLUTION, ARBITRATION.. This Agreement shall be governed by, and construed in accordance with, the laws of the State of California and the United

States, as though made and to be fully performed therein without regard to conflicts of laws principles thereof.

The parties shall initially attempt in good faith to resolve any significant controversy, claim, allegation of breach or dispute arising out of or relating to this Agreement (hereinafter collectively referred to as a "Dispute") through negotiations between senior executives of Watson and Halsey. If the Dispute is not resolved within thirty (30) days (or such other period of time mutually agreed upon by the parties) of notice of the Dispute (the "Executive Resolution Period"), then the parties agree to submit the Dispute to arbitration as provided herein. Unless otherwise mutually agreed by the parties, only if the Dispute is not resolved through negotiations as set forth herein, may a party resort to arbitration.

All Disputes relating in any way to this Agreement shall be resolved exclusively through arbitration conducted in accordance with the Commercial Arbitration Rule of the American Arbitration Association as then in effect. In the event either party demands arbitration, it shall do so within thirty (30) days after the expiration of the Executive Resolution Period (or any mutually agreed extension) and shall include a request that such arbitration be held within thirty (30) days of such demand. The arbitration hearing shall be held as soon as practicable. The arbitration hearing shall be held in Orange County, California and shall be before a single arbitrator selected by the parties in accordance with the Commercial Arbitration Rule of the American Arbitration Association pursuant to its rules on selection of arbitrators. The arbitrator shall render a formal, binding non-appealable resolution and award on each issue as expeditiously as possible but not more than ten (10) business days after the hearing. In any arbitration, the prevailing party shall be entitled to reimbursement of its reasonable attorneys fees and the parties shall use all reasonable efforts to keep arbitration costs to a minimum.

8.9 ATTORNEYS' FEES. Each party shall bear its own legal fees incurred in connection with the transaction that is contemplated hereby, provided, however, that if either party to this Agreement seeks to enforce its rights under this Agreement by legal proceedings or otherwise, the non-prevailing party shall pay all costs and expenses incurred by the prevailing party, including, without limitation, reasonable attorneys' fees.

8.10 SEVERABILITY. To the extent permitted by applicable law, any term or provision of this Agreement which is invalid or unenforceable will be ineffective to the extent of such invalidity or unenforceability without rendering invalid or unenforceable the remaining rights of the Person intended to be benefited by such term or provision or any other provisions of this Agreement.

8.11 ENTIRE AGREEMENT. This Agreement, and all other agreements, certificates, documents and instruments contemplated hereby or thereby (in each case including any Exhibits or Schedules attached hereto or thereto), contains the sole and entire agreement and understanding of the parties hereto and their respective Affiliates and representatives related to the subject matter hereof and supersedes all oral or written agreements concerning the subject matter made prior to the date of this Agreement. There are no agreements, covenants or undertakings with respect to the subject matter of this Agreement or the other agreements, documents, certificates or instruments referred to in this Section 8.11 other than those expressly set forth or referred to herein or therein and no representations or warranties of any kind or nature whatsoever, express or implied, are made or shall be deemed to be made herein by the parties hereto except those expressly made in this Agreement and such other agreements, documents, certificates and instruments.

8.12 PUBLIC ANNOUNCEMENTS. Except to the extent disclosure may be required by applicable law or the rules or regulations of any stock exchange on which such party's stock is traded, neither party shall issue or make any public announcement or press release, or otherwise make any public statement, with respect to this Agreement without obtaining the other party's approval, which approval shall not be unreasonably withheld or delayed. In the event a party determines that applicable law or the rules or regulations of any stock exchange on which such party's stock is listed requires such a disclosure, it shall provide the other party a copy of the intended disclosure and provide such party a reasonable opportunity to comment on such disclosure. Attached as Exhibit E is a form of joint press release describing the material terms of the transactions contemplated by this Agreement. Halsey and Watson intend to release the form of press release attached as Exhibit E on or about the date of execution of this Agreement.

IN WITNESS WHEREOF, the parties have caused this Agreement to be executed by their duly authorized representatives as of the day and year first indicated above.

WATSON PHARMACEUTICALS, INC.

By:/s/ Robert C. Funsten

Name :

Title: Senior Vice President

HALSEY DRUG CO., INC.

By:/s/ Michael Reicher

Name:

Title: Chief Executive

Officer

FINISHED GOODS SUPPLY AGREEMENT
[(_____)]

This Finished Goods Supply Agreement (the "Agreement") dated this 29th day of March, 2000 between Watson Pharmaceuticals, Inc., a Nevada corporation, ("Watson") and Halsey Drug Co., Inc., a New York corporation ("Halsey").

RECITALS

A. Watson and Halsey have entered into a Product Purchase Agreement and an Active Ingredient Supply Agreement, each of even date herewith, pursuant to which (i) Halsey has sold, and Watson has purchased the Product Assets, as defined in the Product Purchase Agreement, relating to an ANDA formulation for [_____] and (ii) Halsey will manufacture and supply to Watson the active pharmaceutical ingredient [_____].

B. Watson and Halsey desire to establish a relationship, pursuant to which Halsey (or its appropriate Affiliates) will supply, and Watson (or its appropriate Affiliates) will purchase, the Commercial Products, as defined herein.

In consideration of the foregoing premises, and the mutual covenants and obligations set forth herein, Halsey and Watson hereby agree as follows:

ARTICLE 1
DEFINITIONS

1.1. "AFFILIATE" shall mean, with respect to any party, any person or entity which, directly or indirectly through one or more intermediaries, controls, is controlled by, or is under common control with, such party. A person or entity shall be deemed to control a corporation (or other entity) if such person or entity possesses, directly or indirectly, the power to direct or cause the direction of the management and policies of such corporation (or other entity) whether through the ownership of voting securities, by contract or otherwise.

1.2. "ANDA" shall mean the Abbreviated New Drug Application No. [____] for [_____] filed with the FDA by Halsey and assigned to Watson or its Affiliate, and any supplements thereto.

1.3. "COMMERCIAL PRODUCTS" shall mean either or both of the NDA and ANDA formulations of [_____] in capsule form for oral administration, packaged, labeled and finished to meet the Commercial Product Specifications, and includes samples and trade packaging.

1.4. "COMMERCIAL PRODUCT SPECIFICATIONS" shall mean the specifications for the relevant Commercial Product set forth in Exhibit A attached hereto, including (as applicable) statements of pharmaceutical manufacturing, Labeling, filling, Packaging, storage and quality control procedures, and labeling and packaging specifications (as such may be revised from time to time in accordance with the terms of this Agreement by written agreement executed by the parties).

1.5. "CONFIDENTIAL INFORMATION" shall mean, with respect to a party, all information of any kind whatsoever (including without limitation, data, compilations, formulae, models, patent disclosures, procedures, processes, projections, protocols, results of experimentation and testing, specifications, strategies and techniques), and all tangible and intangible embodiments thereof of any kind whatsoever (including without limitation, apparatus, compositions, documents, drawings, machinery, patent applications, records and reports), which is disclosed by such party to the other party and is marked, identified as or otherwise acknowledged to be confidential at the time of disclosure to the other party. Notwithstanding the foregoing, Confidential Information of a party shall not include information which the other party can establish by written documentation (a) to have been publicly known prior to disclosure of such information by the disclosing party to the other party, (b) to have become publicly known, without fault on the part of the other party, subsequent to disclosure of such information by the disclosing party to the other party, (c) to have been received by the other party at any time from a source, other than the disclosing party, rightfully having possession of and the right to disclose such information, (d) to have been otherwise known by the other party prior to disclosure of such information by the disclosing party to the other party, or (e) to have been independently developed by employees or agents of the other party without the use of such information disclosed by the disclosing party to the other party.

1.6. "FDA" shall mean the United States Food and Drug Administration, and any successor agency thereto.

1.7. "GMP" shall mean current Good Manufacturing Practices promulgated by the FDA, and their equivalent promulgated by the governing health authority of any other country in which the Commercial Products are manufactured by Halsey under this Agreement.

1.8. "HALSEY INTELLECTUAL PROPERTY" shall mean the Intellectual Property obtained by, or licensed to, Watson under the Product Purchase Agreement.

1.9. "INTELLECTUAL PROPERTY" shall mean Watson's and its Affiliates' rights existing as of the date hereof and as may be developed hereafter in and to all confidential or proprietary information, trade secrets, patent rights, technology, know-how, developments, improvements, techniques, data, methods, processes, instructions, formulae, recipes, drawings and specifications necessary to manufacture and supply the Commercial Product hereunder, and shall include the Halsey Intellectual Property.

1.10. "LABEL", "LABELED" OR "LABELING" shall mean all labels and other written, printed or graphic matter upon (i) the Commercial Product or any container or wrapper utilized with the Commercial Product, or (ii) any written material accompanying the Commercial Product, including, without limitation, package inserts.

1.11. "LIMITED WARRANTY" shall have the meaning defined in Section 2.6(c) hereof.

1.12. "PACKAGING" shall mean all primary containers, including blisters, cartons, shipping cases or any other like matter used in packaging or accompanying the Commercial Products.

1.13. "PERSON" shall mean an individual, corporation, partnership, limited liability company, trust, business trust, association, joint stock company, joint venture, pool, syndicate, sole proprietorship, unincorporated organization, governmental authority or any other form of entity not specifically listed herein.

1.14. RAW MATERIAL COST" shall mean the cost of raw materials used to manufacture the Commercial Products, determined in accordance with generally accepted accounting principles and consistent with Halsey's accounting practices for other products manufactured.

1.15. "REGULATORY DOSSIERS" shall mean all registrations, permits, licenses, authorizations, approvals, presentations, notifications or filings (together with all applications therefor), which are filed with or granted by the governing health authority of any country, and which are required to develop, make, use, sell, import or export the Commercial Products, other than the Drug Master File.

ARTICLE 2 MANUFACTURE, SUPPLY AND PURCHASE

2.1. LICENSE GRANT. Watson hereby grants to Halsey a non-exclusive license to use and practice the Intellectual Property solely to manufacture the Commercial Products for Watson in accordance with the provisions of this Agreement. Watson makes no representation or warranty that the Intellectual Property licensed hereunder is sufficient to allow Halsey to perform its obligations hereunder. Except as provided in this Section 2.1, Halsey acknowledges that it has no intellectual property rights in the Commercial Products.

2.2. SUPPLY AND PURCHASE OBLIGATIONS. During the applicable term of this Agreement, Halsey shall manufacture and supply formulations of [] in capsule form for oral administration exclusively for Watson. Watson shall purchase its requirements of Commercial Product exclusively from Halsey unless Halsey fails to supply conforming Commercial Products as Watson orders pursuant to Section 2.5(c) below (subject to Section 2.5(b) below) for any two (2) out of four (4) consecutive calendar quarters. Watson shall have no obligation to purchase Commercial Products under this Agreement, except to the extent Watson provides to Halsey purchase orders pursuant to Section 2.5(c) below, provided however, that to the extent Watson purchases [] from Halsey pursuant to the Active Ingredient Supply Agreement [()] of even date herewith, it shall not use such [] except to supply Halsey for manufacture of Commercial Products hereunder (subject to Halsey's continued performance under this Agreement and as otherwise permitted under the Active Ingredient Supply Agreement).

2.3. MANUFACTURING PRACTICES.

(a) Commercial Product Specifications. Halsey shall manufacture, fill, package, label and warehouse the Commercial Products in conformity with the Commercial Product Specifications and in accordance with all applicable laws and regulations.

(b) GMP. Halsey shall manufacture the Commercial Products in accordance with GMP and the Drug Master File. Halsey shall advise Watson of any proposed process changes outside the Drug Master File prior to their implementation by Halsey. Watson shall

have the right, at its sole expense, to audit Halsey for compliance with GMP on reasonable notice during normal business hours at least once in each calendar year, and more often in Watson's reasonable discretion.

(c) Active Pharmaceutical Ingredient. Halsey shall use as the active pharmaceutical ingredient [_____] as instructed by Watson and may be either such ingredient manufactured by Halsey or supplied by a third party.

(d) Certificates of Analysis. Halsey shall provide Watson with a certificate of analysis for each shipment of the Commercial Products manufactured and supplied hereunder based upon a reference standard established by Halsey and reasonably acceptable to Watson.

(e) Quality Control Information. Upon the reasonable request of Watson, Halsey shall provide Watson with such information, including analytical and manufacturing documentation, requested by Watson regarding quality control of the Commercial Products supplied hereunder.

(f) Packaging Control. In addition to its obligations pursuant to Sections 2.3(d) and (e), Halsey will evaluate and inspect each batch of Commercial Products in accordance with Packaging guidelines set forth in the Commercial Product Specifications and will provide Watson with a Commercial Product lot release.

(g) Inspection. Watson, or its designee, may, at its own expense, with prior reasonable notice and during regular business hours, visit the facilities used by Halsey to manufacture Commercial Products to review the Commercial Product related records and the facilities.

(h) Technical Requirements. In addition Halsey shall comply with the technical requirements set forth on Exhibit B.

2.4. LABELING AND PACKAGING.

(a) Labeling. Each Commercial Product and all Labeling, advertising and promotional material used in connection therewith, shall conform to the Commercial Product Specifications. Watson shall be responsible for ensuring the accuracy of all information contained on all Labels and Labeling for the Commercial Products and for the compliance of all such Labels and Labeling with applicable law. Should Watson desire or be required to make any change in any such Label or Labeling, Watson shall be responsible for the updating of all artwork and text associated with such change and providing such changes to Halsey or its Affiliates. Halsey shall make all necessary arrangements for such changed Labels or Labeling to be printed and shall provide to Watson printer's proofs for Watson's review. Watson shall promptly either provide Halsey any necessary corrections thereto or notify Halsey of its approval of such proofs. Watson shall reimburse Halsey for the cost of preparing the proofs of such new Labels or Labeling, as well as all other costs associated with such new Labels or Labeling.

(b) Packaging. Halsey shall supply all Packaging and Labels for the Commercial Products under this Agreement and such Packaging and Labels shall be in accordance with the Commercial Product Specifications.

2.5. FORECASTS AND ORDERS.

(a) Forecasts. Not less than forty-five (45) days prior to the first day of each calendar quarter, Watson shall prepare and provide Halsey with a written forecast of the estimated Commercial Product requirements of Watson and its Affiliates for each of the following four (4) calendar quarters. Such forecast shall constitute a binding purchase obligation of Watson with respect to the next upcoming quarter only.

(b) Supply Obligation. Each calendar quarter, Halsey shall be required to manufacture, supply and deliver to Watson such quantities of Commercial Products as Watson orders pursuant to Section 2.5(c) below, up to one hundred and twenty-five percent (125%) of the quantity forecasted for such calendar quarter in the most recent forecast under Section 2.5(a) above. Halsey shall use its commercially reasonable efforts to manufacture, supply and deliver to Watson any quantities of Commercial Products as Watson orders pursuant to Section 2.5(c) below, in excess of one hundred and twenty five percent (125%) of the quantity forecasted for such calendar quarter in the most recent forecast under Section 2.5(a) above. If Halsey becomes aware of any circumstances that may cause Halsey to default in its obligation above to deliver such quantities of conforming Commercial Products as Watson orders for any calendar quarter, Halsey shall give Watson prompt written notice describing such circumstances, together with a proposed course of action to remedy such failure.

(c) Orders. Watson shall make all purchases hereunder by submitting firm purchase orders to Halsey. Each such purchase order shall be in writing in a form reasonably acceptable to Halsey, and shall specify the description of the Commercial Product(s) ordered (e.g. branded or generic product, etc.), the quantity ordered, the price therefor under Section 3.1 below, the place of delivery and the required delivery date therefor, which shall not be less than sixty (60) days after the date of such purchase order. In the event of a conflict between the terms and conditions of any purchase order and this Agreement, the terms and conditions of this Agreement shall prevail.

1.6. DELIVERY AND ACCEPTANCE.

(a) Delivery. All Commercial Products supplied under this Agreement shall be shipped F.O.B. Halsey's place of manufacture to such location as designated by Watson in the applicable purchase order. Watson shall pay all freight, insurance charges, taxes, import and export duties, inspection fees and other charges applicable to the sale and transport of Commercial Products purchased by Watson hereunder. Title and risk of loss and damages to Commercial Products purchased by Watson hereunder shall pass to Watson upon delivery to Watson's designated carrier.

(b) Rejection and Cure. If a shipment of Commercial Products or any portion thereof fails to conform to the applicable Commercial Product Specifications, then Watson shall have the right to reject such nonconforming shipment of Commercial Products or the nonconforming portion thereof, as the case may be. Watson shall give written notice to Halsey of its rejection hereunder, within forty five (45) days after Watson's receipt of such shipment, specifying the grounds for such rejection. The nonconforming shipment of Commercial Products, or the nonconforming portion thereof, shall be held for Halsey's disposition, or shall be

returned to Halsey, in each case at Halsey's expense, as directed by Halsey. Halsey shall use its commercially reasonable efforts to replace each nonconforming shipment of Commercial Products, or the nonconforming portion thereof, with conforming Commercial Products as soon as reasonably practicable after receipt of notice of rejection thereof, and in any event shall do so within forty five (45) days after receipt of notice of rejection thereof.

(c) Warranty. Halsey warrants that (a) Commercial Products manufactured hereunder shall conform with the Commercial Product Specifications; (b) Commercial Products shall be manufactured hereunder in accordance with all applicable laws and regulations, GMP and the Regulatory Dossier; and (c) the manufacture and sale of Commercial Products by Halsey hereunder, and the use thereof by Watson and its Affiliates contemplated hereby, shall not infringe the patent rights of any Person or constitute a misappropriation of the trade secrets or other intellectual property rights of any Person, except for any such infringement or misappropriation arising directly from Halsey's use of Intellectual Property (excluding for purposes hereof, the Halsey Intellectual Property) (collectively, parts (a), (b) and (c) above comprise the "Limited Warranty"). HALSEY MAKES NO OTHER WARRANTIES, EXPRESS OR IMPLIED, WITH RESPECT TO THE COMMERCIAL PRODUCTS INCLUDING, WITHOUT LIMITATION, ANY WARRANTY OF MERCHANTABILITY OR WARRANTY OF FITNESS FOR A PARTICULAR PURPOSE.

(d) Cover. If Halsey fails to timely deliver to Watson the quantity of conforming Commercial Products that Watson orders under any purchase order pursuant to Section 2.5(c) above (subject to the provisions of Section 2.5(b) above), after providing written notice to Halsey, Watson shall have the right to purchase substitute Commercial Products from a third party in substitution for the quantity of conforming Commercial Products which Halsey failed to deliver hereunder. Halsey shall reimburse Watson on demand for the difference between the cost of obtaining such substitute Commercial Products (plus any commercially reasonable charges, expenses or commissions incurred by Watson in connection with effecting cover, and any other reasonable expenses incident to such failure), less the price which would have been due to Halsey for the like quantity of Commercial Products if supplied by Halsey hereunder.

2.7. Samples. For a period of three (3) years from the date hereof Watson shall pay to Halsey a fixed fee of [] on the first (1st) day of each calendar quarter for samples. Such obligations shall commence in the first calendar quarter in which Halsey ships samples to Watson in compliance with this Section 2.7. In consideration thereof, during such period Halsey shall supply Watson such reasonable number of samples of Commercial Products as Watson may order, in such packaging as Watson reasonably specifies.

ARTICLE 3 PRICE AND PAYMENT TERMS

3.1. PRICE. Watson shall purchase from Halsey all Commercial Products which are accepted pursuant to Section 2.6 above at a price equal to []. On each anniversary of the date hereof, Halsey may increase such price to reflect any increase in the Raw Material Cost during the

preceding year. Such new price shall be effective for all orders received by Halsey thirty (30) days after written notice of such increase by Halsey to Watson, such notice, showing in reasonably specific detail the calculation of such increase.

3.2. INVOICING. Upon shipment of Commercial Products to Watson, Halsey shall submit invoices therefor to Watson. Watson shall pay each invoice in full within forty five (45) days after the date of invoice. All payment shall be made in U.S. Dollars.

3.3. SALES AND USE TAXES. Watson shall be solely responsible for the payment of all federal, state, or local sales, use or value-added tax, excise or similar charge, or other tax assessment (other than that assessed against income), assessed or charged on the sale of Commercial Products sold pursuant to this Agreement.

3.4. AUDIT RIGHT. Upon the written request of Watson and not more than once in each calendar year, Halsey shall permit an independent certified public accounting firm, selected by Watson and reasonably acceptable to Halsey to have access during normal business hours to such of the records of Halsey as may be reasonably necessary to verify the accuracy of Halsey's calculation of any price increase hereunder for any period ending not more than twenty-four (24) months prior to the date of such request. The accounting firm shall disclose to Watson only whether the calculations are correct or not and the specific details concerning any discrepancies. If such accounting firm concludes that the price increases was overstated during the audited period, Halsey shall reimburse Watson for the amount overpaid by Watson hereunder for such period within thirty (30) days of the date Watson delivers to Halsey such accounting firm's written report so concluding. The fees and expenses charged by such accounting firm shall be paid by Watson; provided, however, if the audit discloses that the price increase was overstated during the audited period by more than five percent (5%), then Halsey shall pay the reasonable fees and expenses charged by such accounting firm.

ARTICLE 4 FURTHER OBLIGATIONS OF THE PARTIES

4.1. DRUG MASTER FILE, REGULATORY DOSSIERS. Halsey has filed, shall be solely responsible for maintaining, and shall maintain the Drug Master File. Watson shall have the nonexclusive right to reference the Drug Master File in all applicable Regulatory Dossiers for Commercial Products. All such Regulatory Dossiers shall be owned by Watson and Halsey shall have no rights therein except as set forth herein.

4.2. FACILITY QUALIFICATION. Halsey shall, at no cost to Watson, take all such actions to qualify (and thereafter to maintain qualification of) the facility (or facilities) at which Halsey manufactures Commercial Products hereunder, as required under applicable law in the United States and each other country in which Watson has informed Halsey that Watson intends to sell Commercial Products, to enable Watson to obtain and maintain all applicable Regulatory Dossiers for the Commercial Products.

4.3. REGISTRATION ASSISTANCE. Upon the reasonable request of Watson, Halsey promptly shall, at no cost to Watson, provide Watson with such information, samples and technical assistance, and otherwise reasonably cooperate with Watson, in connection with the

preparation, prosecution and maintenance of all applicable Regulatory Dossiers for the Commercial Products.

4.4. RECALL. In the event either party believes it may be necessary to conduct a recall, field correction, market withdrawal, stock recovery, or other similar action with respect to any Commercial Products which were sold by Halsey or its Affiliates to Watson or its Affiliates under this Agreement (a "Recall"), Halsey and Watson shall consult with each other as to how best to proceed, it being understood and agreed that the final decision as to any Recall of any Commercial Product shall be made by Watson; provided, however, that Halsey shall not be prohibited hereunder from taking any action that it is required to take by applicable law. Watson shall bear all costs in connection with any such Recall; provided, however, that Halsey shall reimburse Watson for all reasonable out-of-pocket expenses incurred by Watson in connection with any such Recall attributable to any breach by Halsey hereof, including without limitation, Halsey's failure to manufacture and supply any Commercial Products in accordance with the Limited Warranty.

4.5. FURTHER OBLIGATIONS OF HALSEY. During the term of this Agreement, Halsey shall:

(a) At its own expense, promptly respond to all reasonable inquiries from Watson pertaining to the supply of Commercial Product.

(b) Without limiting the other provisions of this Agreement, use its commercially reasonable efforts at all times to minimize Commercial Product delivery time.

(c) Furnish to Watson current copies of all issued master batch records, procedures, specifications and methods and standard operating procedures related to the Commercial Product and submit to Watson for written approval prior to implementation any and all proposed changes to the same.

(d) Obtain Watson's written approval prior to implementing any proposed change in the suppliers of raw material used in the Commercial Products, containers, Packaging, Labeling, Commercial Product Specifications, manufacturing process, testing or the facilities which are related to the manufacturing of Commercial Products.

(e) Promptly notify Watson of any comments, responses or notices received from the FDA, or other applicable regulatory authorities, which relate to or may impact the Commercial Products or the manufacture of the Commercial Products. At its own cost, obtain and maintain any and all Federal and state regulations and/or licenses with respect to the manufacture, by Halsey, of the Commercial Products.

(f) Provide ongoing technical product and process support with respect to the Commercial Products.

(g) Perform stability studies on at least one commercial batch of each Commercial Product per year and provide copies of such stability reports to Watson.

4.6. FURTHER OBLIGATIONS OF WATSON. During the term of this Agreement, Watson shall:

(a) At its own expense, promptly respond to all reasonable inquiries from Halsey pertaining to the supply of Commercial Products.

(b) Assume all responsibility for maintaining the ANDA and any supplements thereto, including making additional filings with the FDA.

(c) Use commercially reasonable efforts to, at its own cost, obtain and maintain any and all Federal and state Regulatory Dossiers and/or licenses with respect to the marketing, sale and distribution of the Commercial Products.

(d) Promptly notify Halsey of any comments, responses or notices received from the FDA, or other applicable regulatory authorities, which relate to or impact the Commercial Products or the manufacture of the Commercial Products.

ARTICLE 5 REPRESENTATIONS AND WARRANTIES

5.1. REPRESENTATIONS AND WARRANTIES. Each party hereby represents and warrants to the other party as follows:

(a) Corporate Existence. Such party is a corporation duly organized, validly existing and in good standing under the laws of the jurisdiction in which it is incorporated.

(b) Authorization and Enforcement of Obligations. Such party (a) has the corporate power and authority and the legal right to enter into this Agreement and to perform its obligations hereunder, and (b) has taken all necessary corporate action on its part to authorize the execution and delivery of this Agreement and the performance of its obligations hereunder. This Agreement has been duly executed and delivered on behalf of such party, and constitutes a legal, valid, binding obligation, enforceable against such party in accordance with its terms.

(c) Consents. All necessary consents, approvals and authorizations of all governmental authorities and other Persons required to be obtained by such party in connection with its performance of this Agreement have been obtained.

(d) No Conflict. The execution and delivery of this Agreement and the performance of such party's obligations hereunder (a) do not conflict with or violate any requirement of applicable laws or regulations, and (b) do not conflict with, or constitute a default under, any material contractual obligation of such party.

5.2. INSURANCE. Halsey and Watson shall maintain comprehensive general liability insurance, including product liability insurance against claims regarding the manufacture of Commercial Products under this Agreement, in such amounts as it customarily maintains for similar products and activities. Each party shall maintain such insurance during the term of this Agreement and thereafter for so long as it customarily maintains insurance for itself for similar products and activities. Each party shall cause the other party to be named as an additional

insured under such insurance and shall provide the other party proof of such insurance upon request. Each party shall give the other party at least thirty (30) days notice of any cancellation, termination or change in such insurance. Either party may substitute a self insurance program on notice to the other party with information demonstrating the adequacy of such program.

ARTICLE 6 INDEMNIFICATION

6.1. **HALSEY'S INDEMNITY OBLIGATIONS.** Halsey shall defend, indemnify and hold harmless Watson, its Affiliates and their respective successors and permitted assigns (and the respective officers, directors, stockholders, partners and employees of each) from and against any and all losses, liabilities, claims, actions, proceedings, damages and expenses (including without limitation reasonable attorneys' fees and expenses) (herein "Damages") relating to or arising (a) from the manufacture of the Commercial Products, (b) any breach by Halsey or its Affiliates of this Agreement, including without limitation, the failure of the Commercial Products to meet the Limited Warranty or (c) any claims, infringement or misappropriation relating to the Halsey Intellectual Property, provided however, Halsey shall have no obligation to indemnify Watson to the extent such Damages relate Halsey's use of the Intellectual Property (other than the Halsey Intellectual Property).

6.2. **WATSON'S INDEMNITY OBLIGATIONS.** Watson shall defend, indemnify and hold harmless Halsey and its Affiliates, and their respective successors and permitted assigns (and the respective officers, directors, stockholders, partners and employees of each) from and against any and all Damages arising out of (a) the handling, possession, use, marketing, distribution or sale of any Commercial Products by Watson or its Affiliates or any of their distributors or agents following Halsey's or its Affiliate's delivery of the Commercial Products to Watson at Halsey's shipping point, except to the extent such Damages give rise to an indemnification claim of Watson under Section 6.1 above, Section 6.1 of the Active Ingredient Supply Agreement, or Section 7.1 of the Product Purchase Agreement and (b) any claims of infringement or misappropriation relating to the Intellectual Property (other than the Halsey Intellectual Property).

6.3. **INDEMNIFICATION.** A party (the "indemnitee") that intends to claim indemnification under this Article 6 shall notify the other party (the "indemnitor") promptly in writing of any action, claim or liability in respect of which the indemnitee believes it is entitled to claim indemnification, provided that the failure to give timely notice to the indemnitor shall not release the indemnitor from any liability to the indemnitee except to the extent the indemnitor is prejudiced thereby. The indemnitor shall have the right, by notice to the indemnitee, to assume the defense of any such action or claim within the fifteen (15) day period after the indemnitor's receipt of notice of any action or claim with counsel of the indemnitor's choice and at the sole cost of the indemnitor. If the indemnitor so assumes such defense, the indemnitee may participate therein through counsel of its choice, but at the sole cost of the indemnitee. The party not assuming the defense of any such claim shall render all reasonable assistance to the party assuming such defense, and all reasonable out-of-pocket costs of such assistance shall be for the account of the indemnitor. No such claim shall be settled other than by the party defending the same, and then only with the consent of the other party which shall not be unreasonably withheld; provided that the indemnitee shall have no obligation to consent to

any settlement of any such action or claim which imposes on the indemnitee any liability or obligation which cannot be assumed and performed in full by the indemnitor, and the indemnitee shall have no right to withhold its consent to any settlement of any such action or claim if the settlement involves only the payment of money by the indemnitor or its insurer.

6.4. LIMITATIONS ON INDEMNIFICATION. Notwithstanding any contrary provision herein:

(i) no party shall be entitled to indemnification with respect to any claim or suit to the extent such claim or suit results from (a) its own negligence or willful misconduct, or (b) any action to which it has consented in writing; and

(ii) neither party shall be liable to the other for any consequential, incidental or indirect damages, including damages for lost profits, loss of opportunity or use of any kind, suffered by the other party, whether in contract, tort or otherwise.

ARTICLE 7 RELATIONSHIP BETWEEN THE PARTIES

7.1 INDEPENDENT CONTRACTOR. The relationship between Halsey and Watson is solely that of buyer and seller, it being understood that each party is acting as an independent contractor for its own account and this Agreement does not establish a joint venture, agency, partnership or employer/employee relationship between the parties. Neither party shall have authority to conclude contracts or otherwise to act for or bind the other party in any manner, whatsoever, as agent or otherwise. Any and all contracts and agreements entered into by either party shall be for that party's sole account and risk and shall not bind the other party in any respect.

ARTICLE 8 CONFIDENTIALITY AND PUBLIC DISCLOSURE

8.1 CONFIDENTIALITY. Except for literature and information intended for disclosure to customers, and except as may be required to obtain government approval to manufacture, sell or use the Commercial Products, each party will treat as confidential the Confidential Information, and will take all necessary precautions to assure the confidentiality of such information. Each party agrees to return to the other party upon the expiration or termination of this Agreement all Confidential Information acquired from such other party, except as to such information it may be required to retain under applicable law or regulation, and except for one copy of such information to be retained by such party's legal department. Neither party shall, during the period of this Agreement or for three (3) years thereafter, without the other party's express prior written consent use or disclose any such Confidential Information for any purpose other than to carry out its obligations hereunder. Each party, prior to disclosure of such Confidential Information to any employee, consultant or advisor shall ensure that such person is bound in writing to observe the confidentiality provisions of this agreement. The obligations of confidentiality shall not apply to information that the receiving party is required by law or regulation to disclose, provided however that the receiving party shall so notify the disclosing party of its intent and cooperate with the disclosing party on reasonable measures to protect the confidentiality of the information.

8.2 PUBLIC DISCLOSURE. Except for such disclosure as is deemed necessary, in the reasonable judgment of a party, to comply with applicable laws, no announcement, news release, public statement, publication, or presentation relating to the existence of this Agreement, the subject matter hereof, or either party's performance hereunder will be made without the other party's prior written approval, which approval shall not be unreasonably withheld. The parties agree that they will use reasonable efforts to coordinate the initial announcement or press release relating to the existence of this Agreement so that such initial announcement or press release by each is made contemporaneously.

ARTICLE 9 TERM AND TERMINATION

9.1 TERM. Unless terminated earlier pursuant to Section 9.2 below, the initial term of this Agreement shall expire on the date ten (10) years after the date hereof; provided, however, that the term of this Agreement shall be automatically extended for up to two (2) successive additional terms of five (5) years thereafter unless either party gives to the other not less than one (1) year's written notice of termination prior to the expiration of the initial term, or any additional term, of this Agreement.

9.2 TERMINATION.

(a) By Either Party. A party shall have the right to terminate this Agreement, upon or after the breach of any material provision of this Agreement by the other party if the other party has not cured such breach within sixty (60) days after receipt of written notice thereof from the non-breaching party.

(b) By Watson. Watson shall have the right to terminate this Agreement, on sixty (60) days written notice to Halsey, if Halsey fails to deliver to Watson such quantities of conforming Commercial Products as Watson orders pursuant to Section 2.5(c) above (subject to the provisions of Section 2.5(b) above) for any four (4) out of eight (8) consecutive calendar quarters.

(c) Effect of Expiration and Termination. Expiration or termination of this Agreement shall not relieve the parties of any obligation accruing prior to such expiration or termination. The provisions of Sections 4.4, and 5.2 and Articles 6 and 8 shall survive any expiration or termination of this Agreement. Upon termination or expiration, each party shall immediately deliver to the other (and cause any of its employees, agents or representatives to so deliver), at such party's expense, all Confidential Information of the other party, including without limitation any and all copies, duplications, summaries and/or notes thereof or derived therefrom, regardless of the format.

ARTICLE 10 MISCELLANEOUS

10.1 NOTICES. All notices or other communications given pursuant hereto by one party hereto to the other party shall be in writing and deemed given (a) when delivered by messenger, (b) when sent by telecopier, (with receipt confirmed), (c) when received by the addressee, if sent by Express Mail, Federal Express or other express delivery service (receipt requested), or (d) five

days after being mailed in the U.S., first-class postage prepaid, registered or certified, in each case to the appropriate addresses and telecopier numbers set forth below (or to such other addresses and telecopier numbers as a party may designate as to itself by notice to the other party):

If to Watson, to it at:

Watson Pharmaceuticals, Inc.
311 Bonnie Circle
Corona, CA 92880
Attention: Chief Operating Officer
Telecopier: (909) 270-1429

with a copy to:

Watson Pharmaceuticals, Inc.
311 Bonnie Circle
Corona, CA 92880
Attention: General Counsel
Telecopier No.: (909) 279-8094

If to Halsey, to it at:

Halsey Drug Company, Inc.
695 N. Perryville Road
Rockford, Illinois 61107
Attention: Chief Executive Officer
Telecopier No.: (815) 399-9710

10.2 ASSIGNMENT. Neither party shall, without the prior written consent (not to be unreasonably withheld or delayed) of the other party having been obtained, assign or transfer this Agreement to any person or entity, in whole or in part, provided that, each party may assign or transfer this Agreement to any Affiliate or to any successor by merger of such party or its pharmaceutical business, or upon a sale of all or substantially all of such parties assets, or the assets of its pharmaceutical business, without the prior written consent of the other party hereto. All of the terms and provisions of this Agreement shall be binding upon and inure to the benefit of and be enforceable by the parties hereto and their respective successors and assigns.

10.3 SEVERABILITY. If any portion of this Agreement is held invalid by a court of competent jurisdiction, such portion shall be deemed to be of no force and effect and the Agreement shall be construed as if such portion had not been included herein, provided however, if the deletion of such provision materially impairs the commercial value of this Agreement to either party, the parties shall attempt to renegotiate such provision in good faith.

10.4 ENTIRE AGREEMENT. This Agreement and all Exhibits attached hereto contain the sole and entire agreement and understanding of the parties hereto and their respective Affiliates

and representatives related to the subject matter hereof and supersede all oral or written agreements concerning the subject matter made prior to the date of this Agreement.

10.5 AMENDMENT; WAIVER. This Agreement cannot be amended, changed, modified or supplemented orally, and no amendment, change, modification or supplement of this Agreement shall be recognized nor have any effect, unless the writing in which it is set forth is signed by Halsey and Watson, nor shall any waiver of any of the provisions of this Agreement be effective unless in writing and signed by the party to be charged therewith. The failure of either party to enforce, at any time, or for any period of time, any provision hereof or the failure of either party to exercise any option herein shall not be construed as a waiver of such provision or option and shall in no way affect that party's right to enforce such provision or exercise such option. No waiver of any provision hereof shall be deemed to be, or shall constitute, a waiver of any other provision, or with respect to any succeeding breach of the same provision.

10.6 GOVERNING LAW, DISPUTE RESOLUTION, ARBITRATION. This Agreement shall be governed by, and construed in accordance with, the laws of the State of California and the United States, as though made and to be fully performed therein without regard to conflicts of laws principles thereof.

The parties shall initially attempt in good faith to resolve any significant controversy, claim, allegation of breach or dispute arising out of or relating to this Agreement (hereinafter collectively referred to as a "Dispute") through negotiations between senior executives of Watson and Halsey. If the Dispute is not resolved within thirty (30) days (or such other period of time mutually agreed upon by the parties) of notice of the Dispute (the "Executive Resolution Period"), then the parties agree to submit the Dispute to arbitration as provided herein. Unless otherwise mutually agreed by the parties, only if the Dispute is not resolved through negotiations as set forth herein, may a party resort to arbitration.

All Disputes relating in any way to this Agreement shall be resolved exclusively through arbitration conducted in accordance with the Commercial Arbitration Rule of the American Arbitration Association as then in effect. In the event either party demands arbitration, it shall do so within thirty (30) days after the expiration of the Executive Resolution Period (or any mutually agreed extension) and shall include a request that such arbitration be held within thirty (30) days of such demand. The arbitration hearing shall be held as soon as practicable. The arbitration hearing shall be held in Orange County, California and shall be before a single arbitrator selected by the parties in accordance with the Commercial Arbitration Rule of the American Arbitration Association pursuant to its rules on selection of arbitrators. The arbitrator shall render a formal, binding non-appealable resolution and award on each issue as expeditiously as possible but not more than ten (10) business days after the hearing. In any arbitration, the prevailing party shall be entitled to reimbursement of its reasonable attorneys fees and the parties shall use all reasonable efforts to keep arbitration costs to a minimum.

10.7 SINGULAR AND PLURAL FORMS. The use herein of the singular form shall also denote the plural form, and the use herein of the plural form shall denote the singular form, as in each case the context may require.

10.8 HEADINGS. The headings contained in this Agreement are for convenience of reference only and shall not constitute a part hereof or define, limit or otherwise affect the meaning of any of the terms or provisions hereof.

10.9 COUNTERPARTS. This Agreement may be executed in one or more counterparts, each of which shall be deemed an original, but all of which, when taken together, shall constitute one and the same instrument.

IN WITNESS WHEREOF, the parties have caused this Agreement to be executed by their respective duly authorized officers as of the date first above written.

WATSON PHARMACEUTICALS, INC.

By:/s/ Robert C. Funsten

Name:

Title: Senior Vice President

HALSEY DRUG CO., INC.

By:/s/ Michael Reicher

Name:

Title: Chief Executive Officer

ACTIVE INGREDIENT SUPPLY AGREEMENT
[(_____)]

This Active Ingredient Supply Agreement (the "Agreement") dated this 29th day of March, 2000 between Watson Pharmaceuticals, Inc., a Nevada corporation, ("Watson") and Halsey Drug Co., Inc., a New York corporation ("Halsey").

RECITALS

A. Watson and Halsey have entered into a Product Purchase Agreement and a Finished Goods Supply Agreement, each of even date herewith, pursuant to which (i) Halsey has sold, and Watson has purchased the Product Assets, as defined in the Product Purchase Agreement, relating to a formulation for [_____] and (ii) Halsey will manufacture and supply to Watson finished pharmaceutical goods containing the active pharmaceutical ingredient [_____] in capsule form for oral administration.

B. Watson and Halsey desire to establish a relationship, pursuant to which Halsey (or its appropriate Affiliates) will supply, and Watson (or its appropriate Affiliates) will purchase, the Active Ingredient (as defined herein).

In consideration of the foregoing premises, and the mutual covenants and obligations set forth herein, Halsey and Watson hereby agree as follows:

ARTICLE 1
DEFINITIONS

1.1. "ACTIVE INGREDIENT" shall mean the active pharmaceutical ingredient [_____].

1.2. "ACTIVE INGREDIENT SPECIFICATIONS" shall mean the specifications for the Active Ingredient set forth in Exhibit A attached hereto, including (as applicable) statements of pharmaceutical manufacturing, filling, storage and quality control procedures, and labeling and packaging specifications (as such may be revised from time to time in accordance with the terms of this Agreement by written agreement executed by the parties). The parties acknowledge that there may be more than one form of Active Ingredient and that each such form will have its own Active Ingredient Specifications.

1.3. "AFFILIATE" shall mean, with respect to any party, any person or entity which, directly or indirectly through one or more intermediaries, controls, is controlled by, or is under common control with, such party. A person or entity shall be deemed to control a corporation (or other entity) if such person or entity possesses, directly or indirectly, the power to direct or cause the direction of the management and policies of such corporation (or other entity) whether through the ownership of voting securities, by contract or otherwise.

1.4. "COMMERCIAL PRODUCT" shall mean a formulation of [] in capsule form for oral administration, packaged, labeled and finished to meet the certain specifications for acceptance set forth by Watson, and includes samples and trade packaging.

1.5. "CONFIDENTIAL INFORMATION" shall mean, with respect to a party, all information of any kind whatsoever (including without limitation, data, compilations, formulae, models, patent disclosures, procedures, processes, projections, protocols, results of experimentation and testing, specifications, strategies and techniques), and all tangible and intangible embodiments thereof of any kind whatsoever (including without limitation, apparatus, compositions, documents, drawings, machinery, patent applications, records and reports), which is disclosed by such party to the other party and is marked, identified as or otherwise acknowledged to be confidential at the time of disclosure to the other party. Notwithstanding the foregoing, Confidential Information of a party shall not include information which the other party can establish by written documentation (a) to have been publicly known prior to disclosure of such information by the disclosing party to the other party, (b) to have become publicly known, without fault on the part of the other party, subsequent to disclosure of such information by the disclosing party to the other party, (c) to have been received by the other party at any time from a source, other than the disclosing party, rightfully having possession of and the right to disclose such information, (d) to have been otherwise known by the other party prior to disclosure of such information by the disclosing party to the other party, or (e) to have been independently developed by employees or agents of the other party without use of such information disclosed by the disclosing party to the other party.

1.6. "DRUG MASTER FILE" shall mean Halsey's Drug Master File for manufacturing the Active Ingredient filed with the FDA, and the equivalent filing with the governing health authority of any other country.

1.7. "FDA" shall mean the United States Food and Drug Administration, and any successor agency thereto.

1.8. "GMP" shall mean current Good Manufacturing Practices promulgated by the FDA, and their equivalent promulgated by the governing health authority of any other country in which the Active Ingredient are manufactured by Halsey under this Agreement.

1.9. "HALSEY INTELLECTUAL PROPERTY" shall mean the Intellectual Property obtained by, or licensed to, Watson under the Product Purchase Agreement.

1.10. "INTELLECTUAL PROPERTY" shall mean Watson's and its Affiliates' rights existing as of the date hereof and as may be developed hereafter in and to all confidential or proprietary information, trade secrets, patent rights, technology, know-how, developments, improvements, techniques, data, methods, processes, instructions, formulas, recipes, drawings and specifications necessary to manufacture and supply the Active Ingredient hereunder, and shall include the Halsey Intellectual Property.

1.11. "LIMITED WARRANTY" shall have the meaning defined in Section 2.5(d) hereof.

1.12. "PERSON" shall mean an individual, corporation, partnership, limited liability company, trust, business trust, association, joint stock company, joint venture, pool, syndicate, sole proprietorship, unincorporated organization, governmental authority or any other form of entity not specifically listed herein.

1.13. "RAW MATERIAL COST" shall mean the cost of raw materials used to manufacture the Active Ingredient, determined in accordance with generally accepted accounting principles and consistent with Halsey's accounting practices for other active ingredients manufactured

1.14. "REGULATORY DOSSIERS" shall mean all registrations, permits, licenses, authorizations, approvals, presentations, notifications or filings (together with all applications therefor), which are filed with or granted by the governing health authority of any country, and which are required to develop, make, use, sell, import or export the Active Ingredient and Commercial Products, other than the Drug Master File.

ARTICLE 2
MANUFACTURE, SUPPLY AND PURCHASE

2.1. LICENSE GRANT. Watson hereby grants to Halsey a non-exclusive license to use and practice the Intellectual Property solely to manufacture the Active Ingredient for Watson in accordance with the provisions of this Agreement. Watson makes no representation or warranty that the Intellectual Property licensed hereunder is sufficient to allow Halsey to perform its obligations hereunder.

2.2. SUPPLY AND PURCHASE OBLIGATIONS. During the applicable term of this Agreement, Halsey shall manufacture and supply Active Ingredient for Watson. However, Watson shall not be entitled to purchase, and Halsey shall have no obligation to supply, Active Ingredient hereunder for manufacture of Commercial Product by a third party which meets the specifications for Commercial Products as set forth in the Finished Goods Supply Agreement [(____)] of even date herewith, and is subject to ANDA No. [____], so long as Halsey is supplying Watson with Finished Goods in accordance with such agreement. Halsey may manufacture and supply Active Ingredient to third parties, provided however that (i) Halsey may not use the Intellectual Property for such purposes, and (ii) in the event of any shortage of Active Ingredient, Halsey shall fill Watson's orders in full prior to filling orders of any third party. Watson shall have no obligation to purchase Active Ingredient under this Agreement, except to the extent Watson provides to Halsey purchase orders pursuant to Section 2.4(c) below.

2.3. MANUFACTURING PRACTICES.

(a) Active Ingredient Specifications. Halsey shall manufacture the Active Ingredient in conformity with the Active Ingredient Specifications and in accordance with all applicable laws and regulations.

(b) GMP. Halsey shall manufacture the Active Ingredient in accordance with GMP and the Drug Master File. Halsey shall advise Watson of any proposed process changes outside the Drug Master File prior to their implementation by Halsey. Watson shall have the right, at its sole expense, to audit Halsey for compliance with GMP on reasonable notice during normal business hours at least once in each calendar year, and more often in Watson's reasonable discretion.

(c) Certificates of Analysis. Halsey shall provide Watson with a certificate of analysis for each shipment of Active Ingredient manufactured and supplied hereunder based upon a reference standard established by Halsey and reasonably acceptable to Watson.

(d) Quality Control Information. Upon the reasonable request of Watson, Halsey shall provide Watson with such information, including analytical and manufacturing documentation, requested by Watson regarding quality control of Active Ingredient supplied hereunder.

(e) Inspection. Watson, or its designee, may, at its own expense, with prior reasonable notice and during regular business hours, visit the facilities used by Halsey to manufacture Active Ingredient to review the Active Ingredient related records and the facilities.

(f) Technical Requirements. In addition Halsey shall comply with the technical requirements set forth on Exhibit B.

2.4. FORECASTS AND ORDERS.

(a) Forecasts. Not less than forty-five (45) days prior to the first day of each calendar quarter, Watson shall prepare and provide Halsey with a written forecast of the estimated Active Ingredient requirements of Watson and its Affiliates for each of the following four (4) calendar quarters. Such forecast shall constitute a binding purchase obligation of Watson with respect to the first quarter thereof, and the rest of such forecast shall be non-binding.

(b) Supply Obligation. Each calendar quarter, Halsey shall be required to manufacture, supply and deliver to Watson such quantities of Active Ingredient as Watson orders pursuant to Section 2.4(c) below, up to one hundred and twenty five percent (125%) of the quantity forecasted for such calendar quarter in the most recent forecast under Section 2.4(a) above. Halsey shall use its commercially reasonable efforts to manufacture, supply and deliver to Watson any quantities of Active Ingredient as Watson orders pursuant to Section 2.4(c) below, in excess of one hundred and twenty five percent (125%) of the quantity forecasted for such calendar quarter in the most recent forecast under Section 2.4(a) above, and shall fill all of Watson's orders (for Active Ingredient or finished goods order by Watson under the Finished Goods Supply Agreement, as determined by Watson) prior to filling orders of any third party for Active Ingredient. If Halsey becomes aware of any circumstances that may cause Halsey to default in its obligation above to deliver such quantities of conforming Active Ingredient as Watson orders for any calendar quarter, Halsey shall give Watson prompt written notice describing such circumstances, together with a proposed course of action to remedy such failure.

(c) Orders. Watson shall make all purchases hereunder by submitting firm purchase orders to Halsey. Each such purchase order shall be in writing in a form reasonably acceptable to Halsey, and shall specify the form of Active Ingredient ordered, the quantity ordered, the price therefor under Section 3.1 below, the place of delivery and the required delivery date therefor, which shall not be less than sixty (60) days after the date of such purchase order. In the event of a conflict between the terms and conditions of any purchase order and this Agreement, the terms and conditions of this Agreement shall prevail.

1.5. DELIVERY AND ACCEPTANCE.

(a) Delivery. All Active Ingredient supplied under this Agreement shall be shipped F.O.B. Halsey's place of manufacture to such location as designated by Watson (which may be a Watson facility or the facility of a contractor of Watson) in the applicable purchase order. Watson shall pay all freight, insurance charges, taxes, import and export duties, inspection fees and other charges applicable to the sale and transport of Active Ingredient purchased by Watson hereunder. Title and risk of loss and damages to Active Ingredient purchased by Watson hereunder shall pass to Watson upon delivery to Watson's designated carrier.

(b) Rejection and Cure. If a shipment of Active Ingredient or any portion thereof fails to conform to the Active Ingredient Specifications, then Watson shall have the right to reject such nonconforming shipment of Active Ingredient or the nonconforming portion thereof, as the case may be. Watson shall give written notice to Halsey of its rejection hereunder, within forty five (45) days after Watson's receipt of such shipment, specifying the grounds for such rejection. The nonconforming shipment of Active Ingredient, or the nonconforming portion thereof, shall be held for Halsey's disposition, or shall be returned to Halsey, in each case at Halsey's expense, as directed by Halsey. Halsey shall use its commercially reasonable efforts to replace each nonconforming shipment of Active Ingredient, or the nonconforming portion thereof, with conforming Active Ingredient as soon as reasonably practicable after receipt of notice of rejection thereof, and in any event shall do so within forty five (45) days after receipt of notice of rejection thereof.

(c) Packaging. Halsey shall supply Active Ingredient under this Agreement in labeled bulk containers reasonably acceptable to Watson.

(d) Warranty. Halsey warrants that (a) Active Ingredient manufactured hereunder shall conform with the Active Ingredient Specifications; (b) Active Ingredient shall be manufactured hereunder in accordance with all applicable laws and regulations, GMP and the Drug Master File; and (c) the manufacture and sale of Active Ingredient by Halsey hereunder, and the use thereof by Watson and its Affiliates contemplated hereby, shall not infringe the patent rights of any Person or constitute a misappropriation of the trade secrets or other intellectual property rights of any Person, except for any such infringement or misappropriation arising directly from Halsey's use of the Intellectual Property (excluding, for purposes hereof, the Halsey Intellectual Property) (collectively, parts (a), (b) and (c) above comprise the "Limited Warranty"). HALSEY MAKES NO OTHER WARRANTIES, EXPRESS OR IMPLIED, WITH RESPECT TO THE ACTIVE INGREDIENT, INCLUDING, WITHOUT LIMITATION, ANY WARRANTY OF MERCHANTABILITY OR WARRANTY OF FITNESS FOR A PARTICULAR PURPOSE.

(e) Cover. If Halsey fails to timely deliver to Watson the quantity of conforming Active Ingredient that Watson orders under any purchase order pursuant to Section 2.4(c) above (subject to the provisions of Section 2.4(b) above), after providing written notice to Halsey, Watson shall have the right to purchase substitute Active Ingredient from a third party in substitution for the quantity of conforming Active Ingredient which Halsey failed to deliver hereunder. Halsey shall reimburse Watson on demand for the difference between the cost of obtaining such substitute Active Ingredient (plus any commercially reasonable charges, expenses or commissions incurred by Watson in connection with effecting cover, and any other reasonable expenses incident to such failure), less the price which would have been due to Halsey for the like quantity of Active Ingredient if supplied by Halsey hereunder.

ARTICLE 3
PRICE AND PAYMENT TERMS

3.1. PRICE. Watson shall purchase from Halsey all Active Ingredient which are accepted pursuant to Section 2.5 above at a price of [_____] per [_____] on each anniversary of the date hereof, Halsey may increase such price to reflect any increase in the Raw Material Costs during the preceding year. Such new price shall be effective for all orders received by Halsey thirty (30) days after written notice of such increase by Halsey to Watson, such notice, showing in reasonably specific detail the calculation of such increase.

3.2. INVOICING. Upon shipment of Active Ingredient to Watson, Halsey shall submit invoices therefor to Watson. Watson shall pay each invoice in full within forty five (45) days after the date of invoice. All payment shall be made in U.S. Dollars.

3.3. SALES AND USE TAXES. Watson shall be solely responsible for the payment of all federal, state, or local sales, use or value-added tax, excise or similar charge, or other tax assessment (other than that assessed against income), assessed or charged on the sale of Active Ingredient sold pursuant to this Agreement.

3.4. AUDIT RIGHT. Upon the written request of Watson and not more than once in each calendar year, Halsey shall permit an independent certified public accounting firm, selected by Watson and reasonably acceptable to Halsey to have access during normal business hours to such of the records of Halsey as may be reasonably necessary to verify the accuracy of Halsey's calculation of any price increase hereunder for any period ending not more than twenty-four (24) months prior to the date of such request. The accounting firm shall disclose to Watson only whether the calculations are correct or not and the specific details concerning any discrepancies. If such accounting firm concludes that the price increase was overstated during the audited period, Halsey shall reimburse Watson for the amount overpaid by Watson hereunder for such period within thirty (30) days of the date Watson delivers to Halsey such accounting firm's written report so concluding. The fees and expenses charged by such accounting firm shall be paid by Watson; provided, however, if the audit discloses that the price increase was overstated during the audited period by more than five percent (5%), then Halsey shall pay the reasonable fees and expenses charged by such accounting firm.

ARTICLE 4
FURTHER OBLIGATIONS OF THE PARTIES

4.1. DRUG MASTER FILE. Halsey has filed, shall be solely responsible for maintaining, and shall maintain, the Drug Master File. Watson shall have the nonexclusive right to reference the Drug Master File in all applicable Regulatory Dossiers for Commercial Products. All such Regulatory Dossiers shall be owned by Watson and Halsey shall have no rights therein except as set forth herein.

4.2. FACILITY QUALIFICATION. Halsey shall, at no cost to Watson, take all such actions to qualify (and thereafter to maintain qualification of) the facility (or facilities) at which Halsey manufactures Active Ingredient hereunder, as required under applicable law in the United States and each other country in which Watson has informed Halsey that Watson intends to sell Commercial Products incorporating the Active Ingredient, to enable Watson to obtain and maintain all applicable Regulatory Dossiers for the Commercial Products.

4.3. REGISTRATION ASSISTANCE. Upon the reasonable request of Watson, Halsey promptly shall, at no cost to Watson, provide Watson with such information, samples and technical assistance, and otherwise reasonably cooperate with Watson, in connection with the preparation, prosecution and maintenance of all applicable Regulatory Dossiers for the Active Ingredient.

4.4. RECALL. In the event either party believes it may be necessary to conduct a recall, field correction, market withdrawal, stock recovery, or other similar action with respect to any Commercial Product containing an Active Ingredient which was sold by Halsey or its Affiliates to Watson or its Affiliates under this Agreement (a "Recall"), Halsey and Watson shall consult with each other as to how best to proceed, it being understood and agreed that the final decision as to any Recall of any such Commercial Product shall be made by Watson; provided, however, that Halsey shall not be prohibited hereunder from taking any action that it is required to take by applicable law. Watson shall bear all costs in connection with any such Recall; provided, however, that Halsey shall reimburse Watson for all reasonable out-of-pocket expenses incurred by Watson in connection with any such Recall attributable to any breach by Halsey hereof, including without limitation, Halsey's failure to manufacture and supply any Active Ingredient in accordance with the Limited Warranty.

4.5. FURTHER OBLIGATIONS OF HALSEY. During the term of this Agreement, Halsey shall:

(a) At its own expense, promptly respond to all reasonable inquiries from Watson pertaining to the supply of Active Ingredient.

(b) Without limiting the other provisions of this Agreement, use its commercially reasonable efforts at all times to minimize Active Ingredient delivery time.

(c) Furnish to Watson current copies of all issued master batch records, procedures, specifications and methods and standard operating procedures related to the Active Ingredient and submit to Watson for written approval prior to implementation any and, all proposed changes to the same.

(d) Promptly notify Watson and the FDA of any change in the manufacturing process that may affect the quality or safety of the Active Ingredient; provided however, if such change would materially affect Watson's business, Watson and Halsey shall mutually agree to a schedule for such change.

(e) Promptly notify Watson of any comments, responses or notices received from the FDA, or other applicable regulatory authorities, which relate to or may impact the Active Ingredient or the manufacture of Active Ingredient. At its own cost, obtain and maintain any and all Federal and state regulations and/or licenses with respect to the manufacture, by Halsey, of the Active Ingredient.

(f) Provide ongoing technical product and process support with respect to the Active Ingredient.

4.6. FURTHER OBLIGATIONS OF WATSON. During the term of this Agreement, Watson shall:

(a) At its own expense, promptly respond to all reasonable inquiries from Halsey pertaining to the supply of Active Ingredient.

(b) Promptly notify Halsey of any comments, responses or notices received from the FDA, or other applicable regulatory authorities, which relate to or may impact the Active Ingredient or the manufacture of the Active Ingredient by Halsey.

ARTICLE 5 REPRESENTATIONS AND WARRANTIES

5.1. REPRESENTATIONS AND WARRANTIES. Each party hereby represents and warrants to the other party as follows:

(a) Corporate Existence. Such party is a corporation duly organized, validly existing and in good standing under the laws of the jurisdiction in which it is incorporated.

(b) Authorization and Enforcement of Obligations. Such party (a) has the corporate power and authority and the legal right to enter into this Agreement and to perform its obligations hereunder, and (b) has taken all necessary corporate action on its part to authorize the execution and delivery of this Agreement and the performance of its obligations hereunder. This Agreement has been duly executed and delivered on behalf of such party, and constitutes a legal, valid, binding obligation, enforceable against such party in accordance with its terms.

(c) Consents. All necessary consents, approvals and authorizations of all governmental authorities and other Persons required to be obtained by such party in connection with its performance of this Agreement have been obtained.

(d) No Conflict. The execution and delivery of this Agreement and the performance of such party's obligations hereunder (a) do not conflict with or violate any requirement of applicable laws or regulations, and (b) do not conflict with, or constitute a default under, any material contractual obligation of such party.

5.2. INSURANCE. Halsey and Watson shall maintain comprehensive general liability insurance, including product liability insurance against claims regarding the manufacture of Active Ingredient under this Agreement, in such amounts as it customarily maintains for similar products and activities. Each party shall maintain such insurance during the term of this Agreement and thereafter for so long as it customarily maintains insurance for itself for similar products and activities. Each party shall cause the other party to be named as an additional insured under such insurance and shall provide the other party proof of such insurance upon request. Each party shall give the other party at least thirty (30) days notice of any cancellation, termination or change in such insurance. Either party may substitute a self insurance program on notice to the other party with information demonstrating the adequacy of such program.

ARTICLE 6 INDEMNIFICATION

6.1. HALSEY'S INDEMNITY OBLIGATIONS. Halsey shall defend, indemnify and hold harmless Watson, its Affiliates and their respective successors and permitted assigns (and the respective officers, directors, stockholders, partners and employees of each) from and against any and all losses, liabilities, claims, actions, proceedings, damages and expenses (including without limitation reasonable attorneys' fees and expenses) (herein "Damages") relating to or arising (a) from the manufacture of the Active Ingredient, (b) any breach by Halsey or its Affiliates of this Agreement,

including without limitation, the failure of the Commercial Products to meet the Limited Warranty or (c) any claims, infringement or misappropriation relating to the Halsey Intellectual Property, provided however, Halsey shall have no obligation to indemnify Watson to the extent such Damages relate to Halsey's use of the Intellectual Property (other than the Halsey Intellectual Property).

6.2. WATSON'S INDEMNITY OBLIGATIONS. Watson shall defend, indemnify and hold harmless Halsey and its Affiliates, and their respective successors and permitted assigns (and the respective officers, directors, stockholders, partners and employees of each) from and against any and all Damages arising out of (a) the handling, possession, use, marketing, distribution or sale of any Commercial Products containing Active Ingredient supplied hereunder by Watson or its Affiliates or any of their distributors or agents, except to the extent such Damages give rise to an indemnification claim of Watson under Section 6.1 above, Section 6.1 of the Finished Goods Supply Agreement, or Section 7.1 of the Product Purchase Agreement and (b) any claims of infringement or misappropriation relating to the Intellectual Property (other than the Halsey Intellectual Property).

6.3. INDEMNIFICATION. A party (the "indemnitee") that intends to claim indemnification under this Article 6 shall notify the other party (the "indemnitor") promptly in writing of any action, claim or liability in respect of which the indemnitee believes it is entitled to claim indemnification, provided that the failure to give timely notice to the indemnitor shall not release the indemnitor from any liability to the indemnitee except to the extent the indemnitor is prejudiced thereby. The indemnitor shall have the right, by notice to the indemnitee, to assume the defense of any such action or claim within the fifteen (15) day period after the indemnitor's receipt of notice of any action or claim with counsel of the indemnitor's choice and at the sole cost of the indemnitor. If the indemnitor so assumes such defense, the indemnitee may participate therein through counsel of its choice, but at the sole cost of the indemnitee. The party not assuming the defense of any such claim shall render all reasonable assistance to the party assuming such defense, and all reasonable out-of-pocket costs of such assistance shall be for the account of the indemnitor. No such claim shall be settled other than by the party defending the same, and then only with the consent of the other party which shall not be unreasonably withheld; provided that the indemnitee shall have no obligation to consent to any settlement of any such action or claim which imposes on the indemnitee any liability or obligation which cannot be assumed and performed in full by the indemnitor, and the indemnitee shall have no right to withhold its consent to any settlement of any such action or claim if the settlement involves only the payment of money by the indemnitor or its insurer.

6.4. LIMITATIONS ON INDEMNIFICATION. Notwithstanding any contrary provision herein:

(i) no party shall be entitled to indemnification with respect to any claim or suit to the extent such claim or suit results from (a) its own negligence or willful misconduct, or (b) any action to which it has consented in writing; and

(ii) neither party shall be liable to the other for any consequential, incidental or indirect damages, including damages for lost profits, loss of opportunity or use of any kind, suffered by the other party, whether in contract, tort or otherwise.

ARTICLE 7 RELATIONSHIP BETWEEN THE PARTIES

7.1. INDEPENDENT CONTRACTOR. The relationship between Halsey and Watson is solely that of buyer and seller, it being understood that each party is acting as an independent contractor for

its own account and this Agreement does not establish a joint venture, agency, partnership or employer/employee relationship between the parties. Neither party shall have authority to conclude contracts or otherwise to act for or bind the other party in any manner, whatsoever, as agent or otherwise. Any and all contracts and agreements entered into by either party shall be for that party's sole account and risk and shall not bind the other party in any respect.

ARTICLE 8 CONFIDENTIALITY AND PUBLIC DISCLOSURE

8.1. CONFIDENTIALITY. Except for literature and information intended for disclosure to customers, and except as may be required to obtain government approval to manufacture, sell or use the Commercial Products or Active Ingredient, each party will treat as confidential the Confidential Information, and will take all necessary precautions to assure the confidentiality of such information. Each party agrees to return to the other party upon the expiration or termination of this Agreement all Confidential Information acquired from such other party, except as to such information it may be required to retain under applicable law or regulation, and except for one copy of such information to be retained by such party's legal department. Neither party shall, during the period of this Agreement or for three (3) years thereafter, without the other party's express prior written consent use or disclose any such Confidential Information for any purpose other than to carry out its obligations hereunder. Each party, prior to disclosure of such Confidential Information to any employee, consultant or advisor shall ensure that such person is bound in writing to observe the confidentiality provisions of this Agreement. The obligations of confidentiality shall not apply to information that the receiving party is required by law or regulation to disclose, provided however that the receiving party shall so notify the disclosing party of its intent and cooperate with the disclosing party on reasonable measures to protect the confidentiality of the information.

8.2. PUBLIC DISCLOSURE. Except for such disclosure as is deemed necessary, in the reasonable judgment of a party, to comply with applicable laws, no announcement, news release, public statement, publication, or presentation relating to the existence of this Agreement, the subject matter hereof, or either party's performance hereunder will be made without the other party's prior written approval, which approval shall not be unreasonably withheld. The parties agree that they will use reasonable efforts to coordinate any initial announcement or press release relating to the existence of this Agreement so that such initial announcement or press release by each is made contemporaneously.

ARTICLE 9 TERM AND TERMINATION

9.1. TERM. Unless terminated earlier pursuant to Section 9.2 below, the initial term of this Agreement shall expire on the date ten (10) years after the date hereof; provided, however, that the term of this Agreement shall be automatically extended for up to two (2) successive additional terms of five (5) years each thereafter unless either party gives to the other not less than one (1) year's written notice of termination prior to the expiration of the initial term, or any additional term, of this Agreement.

9.2. TERMINATION.

(a) By Either Party. A party shall have the right to terminate this Agreement, upon or after the breach of any material provision of this Agreement by the other party if the other

party has not cured such breach within sixty (60) days after receipt of written notice thereof from the non-breaching party.

(b) By Watson. Watson shall have the right to terminate this Agreement, on sixty (60) days written notice to Halsey, if Halsey fails to deliver to Watson such quantities of conforming Active Ingredient as Watson orders pursuant to Section 2.4(c) above (subject to the provisions of Section 2.4(b) above) for any four (4) out of eight (8) consecutive calendar quarters.

(c) Effect of Expiration and Termination. Expiration or termination of this Agreement shall not relieve the parties of any obligation accruing prior to such expiration or termination. The provisions of Sections 4.4 and 5.2 and Articles 6 and 8 shall survive any expiration or termination of this Agreement. Upon termination or expiration, each party shall immediately deliver to the other (and cause any of its employees, agents or representatives to so deliver), at such party's expense, all Confidential Information of the other party, including without limitation any and all copies, duplications, summaries and/or notes thereof or derived therefrom, regardless of the format.

ARTICLE 10 MISCELLANEOUS

10.1. NOTICES. All notices or other communications given pursuant hereto by one party hereto to the other party shall be in writing and deemed given (a) when delivered by messenger, (b) when sent by telecopier, (with receipt confirmed), (c) when received by the addressee, if sent by Express Mail, Federal Express or other express delivery service (receipt requested), or (d) five days after being mailed in the U.S., first-class postage prepaid, registered or certified, in each case to the appropriate addresses and telecopier numbers set forth below (or to such other addresses and telecopier numbers as a party may designate as to itself by notice to the other party):

If to Watson, to it at:

Watson Pharmaceuticals, Inc.
311 Bonnie Circle
Corona, CA 92880
Attention: Chief Operating Officer
Telecopier: (909) 270-1429

with a copy to:

Watson Pharmaceuticals, Inc.
311 Bonnie Circle
Corona, CA 92880
Attention: General Counsel
Telecopier No.: (909) 279-8094

If to Halsey, to it at:

Halsey Drug Company, Inc.
695 N. Perryville Road
Rockford, Illinois 61107
Attention: Chief Executive Officer
Telecopier No.: (815) 399-9710

10.2. ASSIGNMENT. Neither party shall, without the prior written consent (not to be unreasonably withheld or delayed) of the other party having been obtained, assign or transfer this Agreement to any person or entity, in whole or in part, provided that, each party may assign or transfer this Agreement to any Affiliate or to any successor by merger of such party or its pharmaceutical business, or upon a sale of all or substantially all of such parties assets, or the assets of its pharmaceutical business, without the prior written consent of the other party hereto. All of the terms and provisions of this Agreement shall be binding upon and inure to the benefit of and be enforceable by the parties hereto and their respective successors and assigns.

10.3. SEVERABILITY. If any portion of this Agreement is held invalid by a court of competent jurisdiction, such portion shall be deemed to be of no force and effect and the Agreement shall be construed as if such portion had not been included herein, provided however, if the deletion of such provision materially impairs the commercial value of this Agreement to either party, the parties shall attempt to renegotiate such provision in good faith.

10.4. ENTIRE AGREEMENT. This Agreement and all Exhibits attached hereto contain the sole and entire agreement and understanding of the parties hereto and their respective Affiliates and representatives related to the subject matter hereof and supersede all oral or written agreements concerning the subject matter made prior to the date of this Agreement.

10.5. AMENDMENT; WAIVER. This Agreement cannot be amended, changed, modified or supplemented orally, and no amendment, change, modification or supplement of this Agreement shall be recognized nor have any effect, unless the writing in which it is set forth is signed by Halsey and Watson, nor shall any waiver of any of the provisions of this Agreement be effective unless in writing and signed by the party to be charged therewith. The failure of either party to enforce, at any time, or for any period of time, any provision hereof or the failure of either party to exercise any option herein shall not be construed as a waiver of such provision or option and shall in no way affect that party's right to enforce such provision or exercise such option. No waiver of any provision hereof shall be deemed to be, or shall constitute, a waiver of any other provision, or with respect to any succeeding breach of the same provision.

10.6. GOVERNING LAW, DISPUTE RESOLUTION, ARBITRATION. This Agreement shall be governed by, and construed in accordance with, the laws of the State of California and the United States, as though made and to be fully performed therein without regard to conflicts of laws principles thereof.

The parties shall initially attempt in good faith to resolve any significant controversy, claim, allegation of breach or dispute arising out of or relating to this Agreement (hereinafter collectively referred to as a "Dispute") through negotiations between senior executives of Watson and Halsey. If the Dispute is not resolved within thirty (30) days (or such other period of time mutually agreed upon by the parties) of notice of the Dispute (the "Executive Resolution Period"), then the parties agree to

submit the Dispute to arbitration as provided herein. Unless otherwise mutually agreed by the parties, only if the Dispute is not resolved through negotiations as set forth herein, may a party resort to arbitration.

All Disputes relating in any way to this Agreement shall be resolved exclusively through arbitration conducted in accordance with the Commercial Arbitration Rule of the American Arbitration Association as then in effect. In the event either party demands arbitration, it shall do so within thirty (30) days after the expiration of the Executive Resolution Period (or any mutually agreed extension) and shall include a request that such arbitration be held within thirty (30) days of such demand. The arbitration hearing shall be held as soon as practicable. The arbitration hearing shall be held in Orange County, California and shall be before a single arbitrator selected by the parties in accordance with the Commercial Arbitration Rule of the American Arbitration Association pursuant to its rules on selection of arbitrators. The arbitrator shall render a formal, binding non-appealable resolution and award on each issue as expeditiously as possible but not more than ten (10) business days after the hearing. In any arbitration, the prevailing party shall be entitled to reimbursement of its reasonable attorneys fees and the parties shall use all reasonable efforts to keep arbitration costs to a minimum.

10.7. SINGULAR AND PLURAL FORMS. The use herein of the singular form shall also denote the plural form, and the use herein of the plural form shall denote the singular form, as in each case the context may require.

10.8. HEADINGS. The headings contained in this Agreement are for convenience of reference only and shall not constitute a part hereof or define, limit or otherwise affect the meaning of any of the terms or provisions hereof.

10.9. COUNTERPARTS. This Agreement may be executed in one or more counterparts, each of which shall be deemed an original, but all of which, when taken together, shall constitute one and the same instrument.

IN WITNESS WHEREOF, the parties have caused this Agreement to be executed by their respective duly authorized officers as of the date first above written.

WATSON PHARMACEUTICALS, INC.

By:/s/ Robert C. Funsten
Name:

Title: Senior Vice President

HALSEY DRUG CO., INC.

By:/s/ Michael Reicher
Name:

Title: Chief Executive Officer

RIGHT OF FIRST NEGOTIATION AGREEMENT

This Right of First Negotiation Agreement (the "Agreement") is dated as of March 29, 2000 (the "Effective Date"), between Watson Pharmaceuticals, Inc., a Nevada corporation, ("Watson") and Halsey Drug Co., Inc., a New York corporation, ("Halsey").

RECITALS

A. Halsey owns proprietary know-how and other intellectual property pertaining to certain existing pharmaceutical compounds, and/or the finished goods form thereof and has or is pursuing regulatory approval of these compounds or finished goods.

B. Halsey may develop new pharmaceutical compounds and/or the finished goods form thereof for eventual regulatory approval and commercialization.

C. Watson desires the first right to negotiate to purchase such compounds and/or the finished goods form thereof on terms similar to those set forth in the Form of Active Ingredient Supply Agreement (attached hereto as Exhibit A) or Finished Goods Supply Agreement (attached hereto as Exhibit B).

In consideration of the foregoing premises and of the mutual covenants and obligations set forth herein, the parties hereto agree as follows:

ARTICLE 1

DEFINITIONS

1.1 "AFFILIATES" shall mean, with respect to any party, any person or entity which, directly or indirectly through one or more intermediaries, controls, is controlled by, or is under common control with, such party. A person or entity shall be deemed to control a corporation (or other entity) if such person or entity possesses, directly or indirectly, the power to direct or cause the direction of the management and policies of such corporation (or other entity) whether through the ownership of voting securities, by contract or otherwise.

1.2 "CONFIDENTIAL INFORMATION" shall mean, with respect to a party, all information of any kind whatsoever (including without limitation, data, compilations, formulae, models, patent disclosures, procedures, processes, projections, protocols, results of experimentation and testing, specifications, strategies and techniques), and all tangible and intangible embodiments thereof of any kind whatsoever (including without limitation, apparatus, compositions, documents, drawings, machinery, patent applications, records and reports), which is disclosed by such party to the other party and is marked, identified as or otherwise acknowledged to be confidential at the time of disclosure to the other party. Notwithstanding the foregoing, Confidential Information of a party shall not include information which the other party can establish by written documentation (a) to have been publicly known prior to disclosure of such information by the disclosing party to the other party, (b) to have become publicly known, without fault on the part of the other party, subsequent to disclosure of such information by the disclosing party to the other party, (c) to have been received by the other party at any time from a source, other than the disclosing party, rightfully having possession of and the right to disclose such information, (d) to have been otherwise known by the other party prior to disclosure of such information by the disclosing party to the other party, or (e) to have been

independently developed by employees or agents of the other party without use of such information disclosed by the disclosing party to the other party.

1.3 "ACTIVE INGREDIENTS" shall mean the pharmaceutical compounds listed on Schedule 1.

1.4 "DMF" shall mean Halsey's Drug Master File for manufacturing the Active Ingredient filed with the FDA.

1.5 "FINISHED GOODS" shall mean a pharmaceutical products listed on Schedule 2 packaged, labeled and finished for pharmaceutical use to meet the certain specifications set forth is the regulatory approvals by all requisite governmental authorities to market and sell such product.

1.6 "FDA" shall mean the United States Food and Drug and any successor agency thereto.

1.7 "REGULATORY APPROVAL" shall mean the approvals by all requisite governmental authorities to market and sell Finished Goods in the United States.

1.8 "REGULATORY DOSSIER" shall mean all registrations, permits, licenses, authorizations, approvals, presentations, notifications or filings (together with all applications therefor), which are filed with or granted by the FDA or other governing health authority of any country, and which are required to develop, make, use, sell, import or export the Active Ingredients or the Finished Goods.

ARTICLE 2

RIGHTS OF FIRST NEGOTIATION

2.1 NOTICE. Within fifteen (15) days of (i) receiving Regulatory Approval (including FDA approval of validation batches) for a Finished Good, or (ii) filing a DMF for a Active Ingredient after the Effective Date, Halsey shall notify Watson in writing, identifying the Finished Good or Active Ingredient, the estimated costs thereof, and providing to Watson the Regulatory Dossier for such Finished Good or Active Ingredient (the "Halsey Notice").

2.2 RIGHT OF NEGOTIATION. For a period of thirty (30) days following the receipt of the Halsey Notice for any Finished Good or Active Ingredient (the "Election Period"), Watson shall have the option to notify Halsey of its intent, in writing, to enter into either an Active Ingredient Supply Agreement for such Active Ingredient or a Finished Goods Supply Agreement for such Finished Good (as the case may be), such supply agreement to be in the form attached hereto respectively as Exhibit A or Exhibit B (the "Watson Election Notice"). For a period of sixty (60) days following the receipt of the Watson Election Notice by Halsey (the "Negotiation Period"), the parties will negotiate in good faith only the following terms of either the Active Supply Agreement or the Finished Goods Supply Agreement: price, exclusivity, territory (which in all events will include the United States), minimum purchase requirements and term, in each case taking into consideration actual costs, competitive factors, market conditions, regulatory constraints, and other appropriate matters.

2.3 SUPPLY TO THIRD PARTIES. If (i) prior to the expiration of the Election Period Watson fails to deliver the Watson Election Notice, or (ii) Watson advises Halsey in writing that it does not

desire to enter into either an Active Ingredient Supply Agreement or a finished Goods Supply Agreement for the Active Ingredient or the Finished Good specified in the applicable Halsey Notice, or (iii) Halsey and Watson cannot agree to the negotiable terms of an Active Ingredient Supply Agreement or a Finished Goods Supply Agreement for the Active Ingredient, or Finished Good, by the end of the Negotiation Period, then Halsey may enter into an active ingredient supply agreement or a finished goods supply agreement with a third party, provided that solely in the case of subsection (iii) of this Section 2.3, the terms of the supply arrangement are no less favorable to Halsey, in any material respect (individually or in the aggregate), than those last proposed by Watson to Halsey pursuant to Section 2.2 above.

2.4 TERMINATION OF RIGHT. If prior to the expiration of the Election Period Watson fails to deliver the Watson Election Notice, or (ii) Watson advises Halsey in writing that it does not desire to enter into either an Active Ingredient Supply Agreement or a Finished Goods Supply Agreement for the Active Ingredient or Finished Good specified in the applicable Halsey Notice, then Watson's right of first negotiation relating to Active Ingredient or Finished Good shall terminate.

ARTICLE 3

REPRESENTATIONS, WARRANTIES AND COVENANTS

3.1 HALSEY REPRESENTATIONS AND WARRANTIES. Halsey represents and warrants as of the date hereof as follows:

3.1.1 CORPORATE AUTHORITY. Halsey is a corporation duly organized, validly existing and in good standing under the laws of the State of New York. Halsey has the power and authority to execute and deliver this Agreement, any the instruments to be executed and delivered by it pursuant hereto and to consummate the transactions contemplated hereby. All acts required to be taken by or on the part of Halsey (corporate or otherwise) to authorize the execution, delivery and performance of this Agreement have been duly and properly taken and this Agreement has been duly and promptly executed and delivered by Halsey and constitutes a legal, valid and binding obligation of Halsey, except as enforcement may be limited by applicable bankruptcy, insolvency, reorganization and moratorium laws and other laws of general application affecting enforcement of creditors' rights generally.

3.1.2 NO CONFLICT. The execution, delivery and performance of this Agreement by Halsey will not violate, conflict with or result in a breach of or constitute a default (or event with which the giving of notice, lapse of time or both, would become a default), under any order or decree of any court, administrative agency or governmental authority, the charter documents of Halsey or any agreement, contract or any other instrument to which Halsey or any other Affiliate is a party or to which its or their assets or property may be bound or affected. No approval, authorization, consent or other order or action of or filing with or providing notice to any court, administrative agency, governmental authority or any other third party is required for the execution, delivery or performance of Halsey under this Agreement. Halsey has delivered to Watson an executed copy of the Asset Purchase Agreement with Barr Laboratories, Inc., dated April 16, 1999, granting Barr Laboratories certain non-exclusive rights to purchase the Finished Goods listed on Schedule 2 and in certain circumstances, to reacquire the rights to the Finished Goods.

3.1.3 LITIGATION. There is no pending, or to Halsey's knowledge threatened, litigation that would reasonably be expected to affect adversely its right and ability to perform its obligations under this Agreement.

3.2 WATSON REPRESENTATIONS AND WARRANTIES. Watson represents and warrants as of the date hereof as follows:

3.2.1 CORPORATE AUTHORITY. Watson is a corporation duly organized, validly existing and in good standing under the laws of the State of Nevada. Watson has the power and authority to execute and deliver this Agreement, any the instruments to be executed and delivered by it pursuant hereto and to consummate the transactions contemplated hereby. All acts required to be taken by or on the part of Watson (corporate or otherwise) to authorize the execution, delivery and performance of this Agreement have been duly and properly taken and this Agreement has been duly and promptly executed and delivered by Watson and constitutes a legal, valid and binding obligation of Watson, except as enforcement may be limited by applicable bankruptcy, insolvency, reorganization and moratorium laws and other laws of general application affecting enforcement of creditors' rights generally.

3.2.2 NO CONFLICT. The execution, delivery and performance of this Agreement by Watson will not violate, conflict with or result in a breach of or constitute a default (or event with which the giving of notice, lapse of time or both, would become a default), under any order or decree of any court, administrative agency or governmental authority, the charter documents of Watson or any agreement, contract or any other instrument to which Watson or any other Affiliate is a party or to which its or their assets or property may be bound or affected. No approval, authorization, consent or other order or action of or filing with or providing notice to any court, administrative agency, governmental authority or any other third party is required for the execution, delivery or performance of Watson under this Agreement.

3.2.3 LITIGATION. There is no pending, or to Watson's knowledge threatened, litigation that would reasonably be expected to affect adversely its right and ability to perform its obligations under this Agreement.

ARTICLE 4

CONFIDENTIALITY

4.1 PROTECTION OF CONFIDENTIAL INFORMATION. Watson and Halsey shall:

(a) not disclose any Confidential Information of the other to third parties except to: (i) government authorities; or (ii) such party's Affiliates, consultants or actual or potential contract manufacturers, licensees, distributors, purchasers, joint ventures, clinical investigators or other persons having bona fide business relations with such party, in each case pursuant to a non-disclosure commitment; and

(b) take such precautions as it normally takes with its own confidential and proprietary information to prevent disclosure to third parties of any Confidential Information (except as contemplated above).

ARTICLE 5

TERM AND TERMINATION

5.1 TERM OF AGREEMENT. Unless terminated earlier pursuant to Section 5.2 below, the initial term of this Agreement shall expire on the date ten (10) years after the date hereof; provide however, that the term of this Agreement shall be automatically extended for up to two (2) successive additional terms of five (5) years each thereafter unless either party gives to the other not less than one (1) year's written notice of termination prior to the expiration of the of the initial term, or any additional term, of this Agreement.

5.2 TERMINATION BY MUTUAL AGREEMENT. This Agreement may be terminated by mutual agreement of the parties as evidenced by a writing executed by each party hereto.

5.3 TERMINATION BY HALSEY. If Watson commits a material breach of any term or condition of that certain Product Purchase Agreement dated of even date herewith between Watson and Halsey (the "Product Purchase Agreement"), including, without limitation, Watson's payment obligations under Section 3.1 thereof, and Watson fails to cure such breach within forty-five (45) days after receiving written notice of the breach from Halsey, Halsey shall have the right to terminate this Agreement upon written notice to Watson at the end of such forty-five (45) day period for Watson's uncured breach.

5.4 EFFECT OF EXPIRATION AND TERMINATION. Expiration or termination of this Agreement shall not relieve the parties of any obligations accruing prior to such expiration or termination. The provisions of Article 4 shall survive any expiration or termination of this Agreement. The expiration or termination of this Agreement in accordance with the provisions of this Article 5 shall immediately terminate Halsey's obligations hereunder, including, without limitation, the obligations of Article 2 hereof regardless of whether the parties are then in negotiations relating to any product described in a Halsey Notice. However, in no event shall any such expiration or termination affect or impair any Active Ingredient Supply Agreement or Finished Goods Supply Agreement which the parties may have entered into as a result of this Agreement. Upon termination or expiration, each party shall immediately deliver to the other (and cause any of its employees, agents or representatives to so deliver), at such parties expense, all Confidential Information of the other party, including, without limitation, any and all copies, duplications, summaries and/or notes thereof or derived therefrom, regardless of the format, except to the extent such Confidential Information relates to any Active Ingredient Supply Agreement or Finished Goods Supply Agreement which the parties may have entered into as a result of this Agreement.

ARTICLE 6

MISCELLANEOUS

6.1 INDEPENDENT CONTRACTORS. This Agreement does not constitute Watson as the agent or legal representative of Halsey, nor does it constitute Halsey as the agent or legal representative of Watson. Neither Watson nor Halsey shall have any right or authority to assume or create any obligation or responsibility or vicarious liability, express or implied, on behalf of or in the name of the other, or to bind the other in any manner.

6.2 NOTICES. All notices or other communications given pursuant hereto by one party hereto to the other party shall be in writing and deemed given (a) when delivered by messenger, (b) when sent by telecopier, (with receipt confirmed), (c) when received by the addressee, if sent by Express Mail, Federal Express or other express delivery service (receipt requested), or (d) five days after being mailed in the U.S., first-class postage prepaid, registered or certified, in each case to the appropriate addresses and telecopier numbers set forth below (or to such other addresses and telecopier numbers as a party may designate as to itself by notice to the other party):

If to Watson, to it at:

Watson Pharmaceuticals, Inc.
311 Bonnie Circle
Corona, CA 92880
Attention: Chief Operating Officer
Telecopier No.: (909) 270-1429

with a copy to:

Watson Pharmaceuticals, Inc.
311 Bonnie Circle
Corona, CA 92880
Attention: General Counsel
Telecopier No.: (909) 279-8094

If to Halsey, to it at:

Halsey Drug Company, Inc.
695 N. Perryville Road
Rockford, Illinois 61107
Attention: Chief Executive Officer
Telecopier No.: (805) 399-9710

6.3 FORCE MAJEURE. Neither party shall be responsible or liable to the other hereunder for failure or delay in performance of this Agreement due to any war, fire, accident or other casualty, or any labor disturbance, or act of God or the public enemy, or governmental action or any other contingency beyond such party's reasonable control. In the event of the applicability of this Section, the party affected by such force majeure shall use reasonable efforts, consistent with good business judgment, to eliminate, cure and overcome any of such causes and resume performance of its obligations.

6.4 SUCCESSORS AND ASSIGNS. Neither party shall, without the prior written consent (not to be unreasonably withheld or delayed) of the other party having been obtained, assign or transfer this Agreement to any person or entity, in whole or in part, provided that, each party may assign or transfer this Agreement to any Affiliate or to any successor by merger of such party or its pharmaceutical business, or upon a sale of all or substantially all of such parties assets, or the assets of its pharmaceutical business, without the prior written consent of the other party hereto. All of the

terms and provisions of this Agreement shall be binding upon and inure to the benefit of and be enforceable by the parties hereto and their respective successors and assigns.

6.5 AMENDMENT. This Agreement may be amended only by written agreement of the parties hereto.

6.6 WAIVER. The failure of a party to insist upon strict adherence to any term of this Agreement on any occasion shall not be considered a waiver of that or any other term hereof or deprive that party of the right thereafter to insist upon strict adherence to that term or any other term of this Agreement. Any waiver must be in writing and be signed by the party against whom the waiver is asserted.

6.7 FURTHER ACTIONS. Each party agrees to execute, acknowledge and deliver such further instruments, and to do all such other acts, as may be reasonably necessary or appropriate in order to carry out the purpose and intent of this Agreement.

6.8 GOVERNING LAW, DISPUTE RESOLUTION, ARBITRATION. This Agreement shall be governed by, and construed in accordance with, the laws of the State of California and the United States, as though made and to be fully performed therein without regard to conflicts of laws principles thereof.

The parties shall initially attempt in good faith to resolve any significant controversy, claim, allegation of breach or dispute arising out of or relating to this Agreement (hereinafter collectively referred to as a "Dispute") through negotiations between senior executives of Watson and Halsey. If the Dispute is not resolved within thirty (30) days (or such other period of time mutually agreed upon by the parties) of notice of the Dispute (the "Executive Resolution Period"), then the parties agree to submit the Dispute to arbitration as provided herein. Unless otherwise mutually agreed by the parties, only if the Dispute is not resolved through negotiations as set forth herein, may a party resort to arbitration.

All Disputes relating in any way to this Agreement shall be resolved exclusively through arbitration conducted in accordance with the Commercial Arbitration Rule of the American Arbitration Association as then in effect. In the event either party demands arbitration, it shall do so within thirty (30) days after the expiration of the Executive Resolution Period (or any mutually agreed extension) and shall include a request that such arbitration be held within thirty (30) days of such demand. The arbitration hearing shall be held as soon as practicable. The arbitration hearing shall be held in Orange County, California and shall be before a single arbitrator selected by the parties in accordance with the Commercial Arbitration Rule of the American Arbitration Association pursuant to its rules on selection of arbitrators. The arbitrator shall render a formal, binding non-appealable resolution and award on each issue as expeditiously as possible but not more than ten (10) business days after the hearing. In any arbitration, the prevailing party shall be entitled to reimbursement of its reasonable attorneys fees and the parties shall use all reasonable efforts to keep arbitration costs to a minimum.

6.9 ATTORNEYS' FEES. Each party shall bear its own legal fees incurred in connection with the transaction that is contemplated hereby, provided, however, that if either party to this Agreement seeks to enforce its rights under this Agreement by legal proceedings or otherwise, the non-prevailing party shall pay all costs and expenses incurred by the prevailing party, including, without limitation, reasonable attorneys' fees.

6.10 SEVERABILITY. To the extent permitted by applicable law, any term or provision of this Agreement which is invalid or unenforceable will be ineffective to the extent of such invalidity or unenforceability without rendering invalid or unenforceable the remaining rights of the Person intended to be benefited by such term or provision or any other provisions of this Agreement.

6.11 ENTIRE AGREEMENT. This Agreement, and all other agreements, certificates, documents and instruments contemplated hereby or thereby (in each case including any Exhibits or Schedules attached hereto or thereto), contains the sole and entire agreement and understanding of the parties hereto and their respective Affiliates and representatives related to the subject matter hereof and supersedes all oral or written agreements concerning the subject matter made prior to the date of this Agreement. There are no agreements, covenants or undertakings with respect to the subject matter of this Agreement or the other agreements, documents, certificates or instruments referred to in this Section 6.11 other than those expressly set forth or referred to herein or therein and no representations or warranties of any kind or nature whatsoever, express or implied, are made or shall be deemed to be made herein by the parties hereto except those expressly made in this Agreement and such other agreements, documents, certificates and instruments.

6.12 PUBLIC ANNOUNCEMENTS. Except to the extent disclosure may be required by applicable law or the rules or regulations of any stock exchange on which such party's stock is traded, neither party shall issue or make any public announcement or press release, or otherwise make any public statement, with respect to this Agreement without obtaining the other party's approval, which approval shall not be unreasonably withheld or delayed. In the event a party determines that applicable law or the rules or regulations of any stock exchange on which such party's stock is listed requires such a disclosure, it shall provide the other party a copy of the intended disclosure and provide such party a reasonable opportunity to comment on such disclosure. Attached as Exhibit G to the Product Purchase Agreement is a form of joint press release describing the material terms of the transactions contemplated by the parties. Halsey and Watson intend to release the form of such press release on or about the date of execution of this Agreement.

IN WITNESS WHEREOF, the parties have caused this Agreement to be executed by their duly authorized representatives as of the day and year first indicated above.

WATSON PHARMACEUTICALS, INC.

By:/s/ Robert C. Funsten

Name:

Title: Senior Vice President

HALSEY DRUG CO., INC.

By:/s/ Michael Reicher

Name:

Title: Chief Executive Officer

SCHEDULE 1
ACTIVE INGREDIENTS

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SCHEDULE 2
FINISHED GOODS

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FINISHED GOODS SUPPLY AGREEMENT

("CORE PRODUCTS")

This Finished Goods Supply Agreement (the "Agreement") dated this 29th day of March, 2000, between Watson Pharmaceuticals, Inc., a Nevada corporation, ("Watson") and Halsey Drug Co., Inc., a New York corporation ("Halsey").

RECITALS

A. Watson and Halsey desire to establish a relationship, pursuant to which Halsey (or its Affiliates) will supply, and Watson (or its Affiliates) will purchase, the Commercial Products as defined herein, commencing on the Effective Date.

In consideration of the foregoing premises, and the mutual covenants and obligations set forth herein, Halsey and Watson hereby agree as follows:

ARTICLE 1
DEFINITIONS

1.1. "AFFILIATE" shall mean, with respect to any party, any person or entity which, directly or indirectly through one or more intermediaries, controls, is controlled by, or is under common control with, such party. A person or entity shall be deemed to control a corporation (or other entity) if such person or entity possesses, directly or indirectly, the power to direct or cause the direction of the management and policies of such corporation (or other entity) whether through the ownership of voting securities, by contract or otherwise.

1.2. "ANDA" shall mean each Abbreviated New Drug Application listed on Schedule 1 filed with the FDA by Halsey and any supplements thereto.

1.3. "COMMERCIAL PRODUCTS" shall mean those products listed on Schedule 1, packaged, labeled and finished to meet the relevant Commercial Product Specifications, and includes samples and trade packaging.

1.4. "COMMERCIAL PRODUCT SPECIFICATIONS" shall mean the specifications for the relevant Commercial Product set forth in Exhibit A attached hereto, including (as applicable) statements of pharmaceutical manufacturing, Labeling, filling, Packaging, storage and quality control procedures, and labeling and packaging specifications (as such may be revised from time to time in accordance with the terms of this Agreement by written agreement executed by the parties).

1.5. "CONFIDENTIAL INFORMATION" shall mean, with respect to a party, all information of any kind whatsoever (including without limitation, data, compilations, formulae, models, patent disclosures, procedures, processes, projections, protocols, results of experimentation and testing, specifications, strategies and techniques), and all tangible and intangible embodiments thereof of any kind whatsoever (including without limitation, apparatus, compositions, documents, drawings, machinery, patent applications, records and reports), which is disclosed by

such party to the other party and is marked, identified as or otherwise acknowledged to be confidential at the time of disclosure to the other party. Notwithstanding the foregoing, Confidential Information of a party shall not include information which the other party can establish by written documentation (a) to have been publicly known prior to disclosure of such information by the disclosing party to the other party, (b) to have become publicly known, without fault on the part of the other party, subsequent to disclosure of such information by the disclosing party to the other party, (c) to have been received by the other party at any time from a source, other than the disclosing party, rightfully having possession of and the right to disclose such information, (d) to have been otherwise known by the other party prior to disclosure of such information by the disclosing party to the other party, or (e) to have been independently developed by employees or agents of the other party without the use of such information disclosed by the disclosing party to the other party.

1.6. "EFFECTIVE DATE" shall mean April 1, 2000.

1.7. "FDA" shall mean the United States Food and Drug Administration, and any successor agency thereto.

1.8. "GMP" shall mean current Good Manufacturing Practices promulgated by the FDA, and their equivalent promulgated by the governing health authority of any other country in which the Commercial Products are manufactured by Halsey under this Agreement.

1.9. "INTELLECTUAL PROPERTY" shall mean Halsey's rights existing as of the date hereof and as may be developed hereafter in and to all confidential or proprietary information, trade secrets, patent rights, technology, know-how, developments, improvements, techniques, data, methods, processes, instructions, formulae, recipes, drawings and specifications necessary to manufacture and supply the Commercial Products hereunder.

1.10. "LABEL", "LABELED" OR "LABELING" shall mean all labels and other written, printed or graphic matter upon (i) the Commercial Products or any container or wrapper utilized with the Commercial Product, or (ii) any written material accompanying the Commercial Products, including, without limitation, package inserts.

1.11. "LIMITED WARRANTY" shall have the meaning defined in Section 2.5(c) hereof.

1.12. "PACKAGING" shall mean all primary containers, including blisters, cartons, shipping cases or any other like matter used in packaging or accompanying the Commercial Products.

1.13. "PERSON" shall mean an individual, corporation, partnership, limited liability company, trust, business trust, association, joint stock company, joint venture, pool, syndicate, sole proprietorship, unincorporated organization, governmental authority or any other form of entity not specifically listed herein.

1.14. "RAW MATERIAL COST" shall mean the cost of raw materials used to manufacture the Commercial Products, determined in accordance with generally accepted accounting principles and consistent with Halsey's accounting practices for other products manufactured.

1.15. "REGULATORY DOSSIERS" shall mean all registrations, permits, licenses, authorizations, approvals, presentations, notifications or filings (together with all applications therefor), which are filed with or granted by the governing health authority of any country, and which are required to develop, make, use, sell, import or export the Commercial Products.

1.16. "TERRITORY" shall mean worldwide.

1.17. "TRADEMARKS" shall mean the marks set forth on Schedule 1.

ARTICLE 2
MANUFACTURE, SUPPLY AND PURCHASE

2.1. SUPPLY AND PURCHASE OBLIGATIONS. During the applicable term of this Agreement, and so long as and during the period that Watson satisfies the quarterly minimum obligations set forth in Section 2.5, Halsey shall not manufacture or supply pharmaceutical products containing the active ingredients in the Commercial Products for the indications for which the Commercial Products are approved, for or to any third party. Except as provided in Section 2.6 below, Watson shall have no obligation to purchase Commercial Products under this Agreement, except to the extent Watson provides to Halsey purchase orders pursuant to Section 2.4(c) below.

2.2. MANUFACTURING PRACTICES.

(a) Commercial Product Specifications. Halsey shall manufacture, fill, package, label and warehouse the Commercial Products in conformity with the Commercial Product Specifications and in accordance with all applicable laws and regulations.

(b) GMP. Halsey shall manufacture the Commercial Products in accordance with GMP and the respective Regulatory Dossiers. Halsey shall advise Watson of any proposed process changes outside the respective Regulatory Dossiers prior to their implementation by Halsey. Watson shall have the right, at its sole expense, to audit Halsey for compliance with GMP on reasonable notice during normal business hours at least once in each calendar year, and more often in Watson's reasonable discretion.

(c) Active Pharmaceutical Ingredient. Halsey shall use as the active pharmaceutical ingredients as instructed by Watson and may be either such ingredient manufactured by Halsey or supplied by a third party.

(d) Certificates of Analysis. Halsey shall provide Watson with a certificate of analysis for each shipment of the Commercial Products manufactured and supplied hereunder based upon a reference standard established by Halsey and reasonably acceptable to Watson.

(e) Quality Control Information. Upon the reasonable request of Watson, Halsey shall provide Watson with such information, including analytical and manufacturing documentation, requested by Watson regarding quality control of the Commercial Products supplied hereunder.

(f) Packaging Control. In addition to its obligations pursuant to Sections 2.3(d) and (e), Halsey will evaluate and inspect each batch of Commercial Products in accordance with Packaging guidelines set forth in the Commercial Product Specifications and will provide Watson with a Commercial Product lot release.

(g) Inspection. Watson, or its designee, may, at its own expense, with prior reasonable notice and during regular business hours, visit the facilities used by Halsey to manufacture Commercial Products to review the Commercial Product related records and the facilities.

(h) Technical Requirements. In addition Halsey shall comply with the technical requirements set forth on Exhibit B.

2.3. LABELING AND PACKAGING.

(a) Labeling. Each Commercial Product and all Labeling, advertising and promotional material used in connection therewith, shall include the Trademark, in the manner and to the extent specified in the relevant Commercial Product Specifications. Watson shall be responsible for ensuring the accuracy of all information contained on all Labels and Labeling for the Commercial Products and for the compliance of all such Labels and Labeling with applicable law. Should Watson desire or be required to make any change in any such Label or Labeling, Watson shall be responsible for the updating of all artwork and text associated with such change and providing such changes to Halsey or its Affiliates. Halsey shall make all necessary arrangements for such changed Labels or Labeling to be printed and shall provide to Watson printer's proofs for Watson's review. Watson shall promptly either provide Halsey any necessary corrections thereto or notify Halsey of its approval of such proofs. Watson shall reimburse Halsey for the cost of preparing the proofs of such new Labels or Labeling, as well as all other costs associated with such new Labels or Labeling.

(b) Packaging. Halsey shall supply all Packaging and Labels for the Commercial Products under this Agreement and such Packaging and Labels shall be in accordance with the relevant Commercial Product Specifications.

2.4. FORECASTS AND ORDERS.

(a) Forecasts. Not less than forty-five (45) days prior to the first day of each calendar quarter, Watson shall prepare and provide Halsey with a written forecast of the estimated Commercial Products requirements of Watson and its Affiliates for each of the following four (4) calendar quarters. Such forecast shall be binding only with respect to the first quarter thereof and shall be non-binding for the balance.

(b) Supply Obligation. Each calendar quarter, Halsey shall be required to manufacture, supply and deliver to Watson such quantities of Commercial Products as Watson orders pursuant to Section 2.4(c) below, up to one hundred and twenty-five percent (125%) of the quantity forecasted for such calendar quarter in the most recent forecast under Section 2.4(a) above. Halsey shall use its commercially reasonable efforts to manufacture, supply and deliver to Watson any quantities of Commercial Products as Watson orders pursuant to Section 2.4(c) below, in excess of one hundred and twenty five percent (125%) of the quantity forecasted for

such calendar quarter in the most recent forecast under Section 2.4(a) above. If Halsey becomes aware of any circumstances that may cause Halsey to default in its obligation above to deliver such quantities of conforming Commercial Products as Watson orders for any calendar quarter, Halsey shall give Watson prompt written notice describing such circumstances, together with a proposed course of action to remedy such failure.

(c) Orders. Watson shall make all purchases hereunder by submitting firm purchase orders to Halsey. Each such purchase order shall be in writing in a form reasonably acceptable to Halsey, and shall specify the description of the Commercial Product(s) ordered by NDC#, the quantity ordered, the price therefor under Section 3.1 below, the place of delivery and the required delivery date therefor, which shall not be less than sixty (60) days after the date of such purchase order. In the event of a conflict between the terms and conditions of any purchase order and this Agreement, the terms and conditions of this Agreement shall prevail.

1.5. DELIVERY AND ACCEPTANCE.

(a) Delivery. All Commercial Products supplied under this Agreement shall be shipped F.O.B. Halsey's place of manufacture to such location as designated by Watson in the applicable purchase order. Watson shall pay all freight, insurance charges, taxes, import and export duties, inspection fees and other charges applicable to the sale and transport of Commercial Products purchased by Watson hereunder. Title and risk of loss and damages to Commercial Products purchased by Watson hereunder shall pass to Watson upon delivery to Watson's designated carrier.

(b) Rejection and Cure. If a shipment of Commercial Products or any portion thereof fails to conform to the applicable Commercial Product Specifications, then Watson shall have the right to reject such nonconforming shipment of Commercial Products or the nonconforming portion thereof, as the case may be. Watson shall give written notice to Halsey of its rejection hereunder, within forty five (45) days after Watson's receipt of such shipment, specifying the grounds for such rejection. The nonconforming shipment of Commercial Products, or the nonconforming portion thereof, shall be held for Halsey's disposition, or shall be returned to Halsey, in each case at Halsey's expense, as directed by Halsey. Halsey shall use its commercially reasonable efforts to replace each nonconforming shipment of Commercial Products, or the nonconforming portion thereof, with conforming Commercial Products as soon as reasonably practicable after receipt of notice of rejection thereof, and in any event shall do so within forty five (45) days after receipt of notice of rejection thereof.

(c) Warranty. Halsey warrants that (a) Commercial Products manufactured hereunder shall conform with the Commercial Product Specifications; (b) Commercial Products shall be manufactured hereunder in accordance with all applicable laws and regulations, GMP and the relevant Regulatory Dossier and (c) the manufacture and sale of Commercial Products by Halsey hereunder, and the use thereof by Watson and its Affiliates contemplated hereby, shall not infringe the patent rights of any Person or constitute a misappropriation of the trade secrets or other intellectual property rights of any Person, (collectively, parts (a), (b) and (c) above comprise the "Limited Warranty"). HALSEY MAKES NO OTHER WARRANTIES, EXPRESS OR IMPLIED, WITH RESPECT TO THE COMMERCIAL PRODUCTS

INCLUDING, WITHOUT LIMITATION, ANY WARRANTY OF MERCHANTABILITY OR WARRANTY OF FITNESS FOR A PARTICULAR PURPOSE.

(d) Cover. If Halsey fails to timely deliver to Watson the quantity of conforming Commercial Products that Watson orders under any purchase order pursuant to Section 2.4(c) above (subject to the provisions of Section 2.4(b) above), after providing written notice to Halsey, Watson shall have the right to purchase substitute Commercial Products from a third party in substitution for the quantity of conforming Commercial Products which Halsey failed to deliver hereunder. Halsey shall reimburse Watson on demand for the difference between the cost of obtaining such substitute Commercial Products (plus any commercially reasonable charges, expenses or commissions incurred by Watson in connection with effecting cover, and any other reasonable expenses incident to such failure), less the price which would have been due to Halsey for the like quantity of Commercial Products if supplied by Halsey hereunder.

2.6. QUARTERLY MINIMUM OBLIGATIONS. Provided that Halsey is supplying Commercial Products in accordance with Watson's orders, for a period of eighteen (18) months from the Effective Date, Watson shall purchase an aggregate of Eighteen Million, Three Hundred Sixty Three Thousand Three Hundred Eighty-Six dollars (\$18,363,386) of Commercial Products. If during any quarter (for purposes of this paragraph, quarters shall end on June 30, September 30, December 31 and March 31) Watson fails to purchase and pay for at least Three Million, Sixty Thousand, Five Hundred Sixty-Four dollars (\$3,060,564) of Commercial Products (the "Minimum Obligation"), it shall, within forty-five (45) days of the end of such quarter, purchase and pay for Commercial Products equal to such shortfall. To the extent that Watson has purchased and paid for Commercial Product in excess of aggregate Minimum Obligations to date, it may credit any such excess against any shortfall. During the first six (6) quarters during the term of this Agreement, Watson must satisfy the Minimum Obligations. Thereafter, if Watson fails to satisfy the Minimum Obligations, Halsey's sole remedy shall be the termination of the exclusive supply obligation set forth in Section 2.1 above.

ARTICLE 3 PRICE AND PAYMENT TERMS

3.1. PRICE. Watson shall purchase from Halsey all Commercial Products which are accepted pursuant to Section 2.5 above at the prices on Schedule 1. On each anniversary of the date hereof, Halsey may increase such prices to reflect any increase in the Raw Material Cost during the preceding year. Such new price shall be effective for all orders received by Halsey thirty (30) days after written notice of such increase by Halsey to Watson, such notice, showing in reasonably specific detail the calculation of such increase.

3.2. INVOICING. Upon shipment of Commercial Products to Watson, Halsey shall submit invoices therefor to Watson. Watson shall pay each invoice in full within forty five (45) days after the date of invoice. All payment shall be made in U.S. Dollars.

3.3. SALES AND USE TAXES. Watson shall be solely responsible for the payment of all federal, state, or local sales, use or value-added tax, excise or similar charge, or other tax

assessment (other than that assessed against income), assessed or charged on the sale of Commercial Products sold pursuant to this Agreement.

3.4. AUDIT RIGHTS. Upon the written request of Watson and not more than once in each calendar year, Halsey shall permit an independent certified public accounting firm, selected by Watson and reasonably acceptable to Halsey to have access during normal business hours to such of the records of Halsey as may be reasonably necessary to verify the accuracy of Halsey's calculation of any price increase hereunder for any period ending not more than twenty-four (24) months prior to the date of such request. The accounting firm shall disclose to Watson only whether the calculations are correct or not and the specific details concerning any discrepancies. If such accounting firm concludes that the price increases was overstated during the audited period, Halsey shall reimburse Watson for the amount overpaid by Watson hereunder for such period within thirty (30) days of the date Watson delivers to Halsey such accounting firm's written report so concluding. The fees and expenses charged by such accounting firm shall be paid by Watson; provided, however, if the audit discloses that the price increase was overstated during the audited period by more than five percent (5%), then Halsey shall pay the reasonable fees and expenses charged by such accounting firm.

ARTICLE 4 FURTHER OBLIGATIONS OF THE PARTIES

4.1. REGULATORY DOSSIERS. Halsey has filed and shall be solely responsible for maintaining all Regulatory Dossiers to permit the sale of Commercial Products by Watson.

4.2. FACILITY QUALIFICATION. Halsey shall, at no cost to Watson, take all such actions to qualify (and thereafter to maintain qualification of) the facility (or facilities) at which Halsey manufactures Commercial Products hereunder, as required under applicable law in the United States and each other country in which Watson has informed Halsey that Watson intends to sell Commercial Products, to enable Halsey to obtain and maintain all applicable Regulatory Dossiers for the Commercial Products.

4.3. RECALL. In the event either party believes it may be necessary to conduct a recall, field correction, market withdrawal, stock recovery, or other similar action with respect to any Commercial Products which were sold by Halsey or its Affiliates to Watson or its Affiliates under this Agreement (a "Recall"), Halsey and Watson shall consult with each other as to how best to proceed, it being understood and agreed that the final decision as to any Recall of any Commercial Products shall be made by Watson; provided, however, that Halsey shall not be prohibited hereunder from taking any action that it is required to take by applicable law. Halsey shall bear all costs in connection with any such Recall unless such Recall is attributable to any breach by Watson hereof, to any item for which Watson is required to indemnify Halsey under Section 6.2 hereof or the gross negligence or willful misconduct of Watson.

4.4. FURTHER OBLIGATIONS OF HALSEY. During the term of this Agreement, Halsey shall:

- (i) at its own expense, promptly respond to all reasonable inquiries from Watson pertaining to the supply of Commercial Products;

(ii) without limiting the other provisions of this Agreement, use its commercially reasonable efforts at all times to minimize Commercial Product delivery time;

(iii) furnish to Watson current copies of all issued master batch records, procedures, specifications and methods and standard operating procedures related to each Commercial Product and submit to Watson for written approval prior to implementation any and all proposed changes to the same;

(iv) obtain Watson's written approval prior to implementing any proposed change in the suppliers of raw material used in the Commercial Products, containers, Packaging, Labeling, Commercial Product Specifications, manufacturing process, testing or the facilities which are related to the manufacturing of Commercial Products;

(v) promptly notify Watson of any comments, responses or notices received from the FDA, or other applicable regulatory authorities, which relate to or may impact the Commercial Products or the manufacture of the Commercial Products. At its own cost, obtain and maintain any and all Federal and state regulations and/or licenses with respect to the manufacture, by Halsey, of the Commercial Products;

(vi) provide ongoing technical product and process support with respect to the Commercial Products; and

(vii) perform stability studies on at least one commercial batch of each Commercial Product per year and provide copies of such stability reports to Watson.

4.5. FURTHER OBLIGATIONS OF WATSON. During the term of this Agreement, Watson shall:

(i) at its own expense, promptly respond to all reasonable inquiries from Halsey pertaining to the supply of Commercial Products; and

(ii) promptly notify Halsey of any comments, responses or notices received from the FDA, or other applicable regulatory authorities, which relate to or impact the Commercial Products or the manufacture of the Commercial Products.

4.6. REBATES, REIMBURSEMENTS. Any government mandated rebates or reimbursements with respect to sales of Commercial Products prior to the date hereof shall be for the account of Halsey. Any government mandated rebates or reimbursements with respect to sales of Commercial Products after the date hereof shall be for the account of Watson. The parties shall from time to time, but at least quarterly, remit to the other party any funds necessary to effectuate the foregoing.

ARTICLE 5
REPRESENTATIONS AND WARRANTIES

5.1. REPRESENTATIONS AND WARRANTIES. Each party hereby represents and warrants to the other party as follows:

(a) Corporate Existence. Such party is a corporation duly organized, validly existing and in good standing under the laws of the jurisdiction in which it is incorporated.

(b) Authorization and Enforcement of Obligations. Such party (a) has the corporate power and authority and the legal right to enter into this Agreement and to perform its obligations hereunder, and (b) has taken all necessary corporate action on its part to authorize the execution and delivery of this Agreement and the performance of its obligations hereunder. This Agreement has been duly executed and delivered on behalf of such party, and constitutes a legal, valid, binding obligation, enforceable against such party in accordance with its terms.

(c) Consents. All necessary consents, approvals and authorizations of all governmental authorities and other Persons required to be obtained by such party in connection with its performance of this Agreement have been obtained.

(d) No Conflict. The execution and delivery of this Agreement and the performance of such party's obligations hereunder (a) do not conflict with or violate any requirement of applicable laws or regulations, and (b) do not conflict with, or constitute a default under, any material contractual obligation of such party.

5.2. INSURANCE. Halsey and Watson shall maintain comprehensive general liability insurance, including product liability insurance against claims regarding the manufacture of Commercial Products under this Agreement, in such amounts as it customarily maintains for similar products and activities. Each party shall maintain such insurance during the term of this Agreement and thereafter for so long as it customarily maintains insurance for itself for similar products and activities. Each party shall cause the other party to be named as an additional insured under such insurance and shall provide the other party proof of such insurance upon request. Each party shall give the other party at least thirty (30) days notice of any cancellation, termination or change in such insurance. Either party may substitute a self insurance program on notice to the other party with information demonstrating the adequacy of such program.

ARTICLE 6
INDEMNIFICATION

6.1. HALSEY'S INDEMNITY OBLIGATIONS. Halsey shall defend, indemnify and hold harmless Watson, its Affiliates and their respective successors and permitted assigns (and the respective officers, directors, stockholders, partners and employees of each) from and against any and all losses, liabilities, claims, actions, proceedings, damages and expenses (including without limitation reasonable attorneys' fees and expenses) (herein "Damages") relating to or arising (a) from the manufacture of the Commercial Product, (b) any breach by Halsey or its Affiliates of this Agreement, including without limitation, the failure of the Commercial Products to meet the Limited Warranty or (c) any claims, infringement or misappropriation relating to the Commercial Product.

6.2. WATSON'S INDEMNITY OBLIGATIONS. Watson shall defend, indemnify and hold harmless Halsey and its Affiliates, and their respective successors and permitted assigns (and the respective officers, directors, stockholders, partners and employees of each) from and against any and all Damages arising out of the handling, possession, use, marketing, distribution or sale of any Commercial Products by Watson or its Affiliates or any of their distributors or agents following Halsey's or its Affiliate's delivery of the Commercial Products to Watson at Halsey's shipping point, except to the extent such Damages give rise to an indemnification claim of Watson under Section 6.1 above.

6.3. INDEMNIFICATION. A party (the "indemnitee") that intends to claim indemnification under this Article 6 shall notify the other party (the "indemnitor") promptly in writing of any action, claim or liability in respect of which the indemnitee believes it is entitled to claim indemnification, provided that the failure to give timely notice to the indemnitor shall not release the indemnitor from any liability to the indemnitee except to the extent the indemnitor is prejudiced thereby. The indemnitor shall have the right, by notice to the indemnitee, to assume the defense of any such action or claim within the fifteen (15) day period after the indemnitor's receipt of notice of any action or claim with counsel of the indemnitor's choice and at the sole cost of the indemnitor. If the indemnitor so assumes such defense, the indemnitee may participate therein through counsel of its choice, but at the sole cost of the indemnitee. The party not assuming the defense of any such claim shall render all reasonable assistance to the party assuming such defense, and all reasonable out-of-pocket costs of such assistance shall be for the account of the indemnitor. No such claim shall be settled other than by the party defending the same, and then only with the consent of the other party which shall not be unreasonably withheld; provided that the indemnitee shall have no obligation to consent to any settlement of any such action or claim which imposes on the indemnitee any liability or obligation which cannot be assumed and performed in full by the indemnitor, and the indemnitee shall have no right to withhold its consent to any settlement of any such action or claim if the settlement involves only the payment of money by the indemnitor or its insurer.

6.4. LIMITATIONS ON INDEMNIFICATION. Notwithstanding any contrary provision herein:

(i) no party shall be entitled to indemnification with respect to any claim or suit to the extent such claim or suit results from (a) its own negligence or willful misconduct, or (b) any action to which it has consented in writing; and

(ii) neither party shall be liable to the other for any consequential, incidental or indirect damages, including damages for lost profits, loss of opportunity or use of any kind, suffered by the other party, whether in contract, tort or otherwise.

ARTICLE 7 RELATIONSHIP BETWEEN THE PARTIES

7.1. INDEPENDENT CONTRACTOR. The relationship between Halsey and Watson is solely that of buyer and seller, it being understood that each party is acting as an independent contractor for its own account and this Agreement does not establish a joint venture, agency, partnership or employer/employee relationship between the parties. Neither party shall have authority to

conclude contracts or otherwise to act for or bind the other party in any manner, whatsoever, as agent or otherwise. Any and all contracts and agreements entered into by either party shall be for that party's sole account and risk and shall not bind the other party in any respect.

ARTICLE 8 CONFIDENTIALITY AND PUBLIC DISCLOSURE

8.1. CONFIDENTIALITY. Except for literature and information intended for disclosure to customers, and except as may be required to obtain government approval to manufacture, sell or use the Commercial Products, each party will treat as confidential the Confidential Information, and will take all necessary precautions to assure the confidentiality of such information. Each party agrees to return to the other party upon the expiration or termination of this Agreement all Confidential Information acquired from such other party, except as to such information it may be required to retain under applicable law or regulation, and except for one copy of such information to be retained by such party's legal department. Neither party shall, during the period of this Agreement or for three (3) years thereafter, without the other party's express prior written consent use or disclose any such Confidential Information for any purpose other than to carry out its obligations hereunder. Each party, prior to disclosure of such Confidential Information to any employee, consultant or advisor shall ensure that such person is bound in writing to observe the confidentiality provisions of this agreement. The obligations of confidentiality shall not apply to information that the receiving party is required by law or regulation to disclose, provided however that the receiving party shall so notify the disclosing party of its intent and cooperate with the disclosing party on reasonable measures to protect the confidentiality of the information.

8.2. PUBLIC DISCLOSURE. Except for such disclosure as is deemed necessary, in the reasonable judgment of a party, to comply with applicable laws, no announcement, news release, public statement, publication, or presentation relating to the existence of this Agreement, the subject matter hereof, or either party's performance hereunder will be made without the other party's prior written approval, which approval shall not be unreasonably withheld or delayed. The parties agree that they will use reasonable efforts to coordinate the initial announcement or press release relating to the existence of this Agreement so that such initial announcement or press release by each is made contemporaneously.

ARTICLE 9 TERM AND TERMINATION

9.1. TERM. Unless terminated earlier pursuant to Section 9.2 below, the initial term of this Agreement shall expire on the date ten (10) years after the date hereof; provided, however, that the term of this Agreement shall be automatically extended for up to two (2) successive additional terms of five (5) years each thereafter unless either party gives to the other not less than one (1) year's written notice of termination prior to the expiration of the initial term, or any additional term, of this Agreement.

9.2. TERMINATION.

(a) By Either Party. A party shall have the right to terminate this Agreement, upon or after the breach of any material provision of this Agreement by the other party if the other party has not cured such breach within sixty (60) days after receipt of written notice thereof from the non-breaching party.

(b) By Watson. Watson shall have the right to terminate this Agreement, on a product-by-product basis, on sixty (60) days written notice to Halsey, if Halsey fails to deliver to Watson such quantities of conforming Commercial Products as Watson orders pursuant to Section 2.4(c) above (subject to the provisions of Section 2.5(b) above) for any four (4) out of eight (8) consecutive calendar quarters.

(c) Effect of Expiration and Termination. Expiration or termination of this Agreement shall not relieve the parties of any obligation accruing prior to such expiration or termination. The provisions of Sections 4.3 and 5.2 and Articles 6 and 8 shall survive any expiration or termination of this Agreement. Upon termination or expiration, each party shall immediately deliver to the other (and cause any of its employees, agents or representatives to so deliver), at such party's expense, all Confidential Information of the other party, including without limitation any and all copies, duplications, summaries and/or notes thereof or derived therefrom, regardless of the format.

ARTICLE 10 MISCELLANEOUS

10.1. NOTICES. All notices or other communications given pursuant hereto by one party hereto to the other party shall be in writing and deemed given (a) when delivered by messenger, (b) when sent by telecopier, (with receipt confirmed), (c) when received by the addressee, if sent by Express Mail, Federal Express or other express delivery service (receipt requested), or (d) five days after being mailed in the U.S., first-class postage prepaid, registered or certified, in each case to the appropriate addresses and telecopier numbers set forth below (or to such other addresses and telecopier numbers as a party may designate as to itself by notice to the other party):

If to Watson, to it at:

Watson Pharmaceuticals, Inc.
311 Bonnie Circle
Corona, CA 92880
Attention: Chief Operating Officer
Telecopier: (909) 270-1429

with a copy to:

Watson Pharmaceuticals, Inc.
311 Bonnie Circle
Corona, CA 92880
Attention: General Counsel
Telecopier No.: (909) 279-8094

If to Halsey, to it at:

Halsey Drug Company, Inc.
695 N. Perryville Road
Rockford, Illinois 61107
Attention: Chief Executive Officer
Telecopier No.: (815) 399-9710

10.2. ASSIGNMENT. Neither party shall, without the prior written consent (not to be unreasonably withheld or delayed) of the other party having been obtained, assign or transfer this Agreement to any person or entity, in whole or in part, provided that, each party may assign or transfer this Agreement to any Affiliate or to any successor by merger of such party or its pharmaceutical business, or upon a sale of all or substantially all of such parties assets, or the assets of its pharmaceutical business, without the prior written consent of the other party hereto. All of the terms and provisions of this Agreement shall be binding upon and inure to the benefit of and be enforceable by the parties hereto and their respective successors and assigns.

10.3. SEVERABILITY. If any portion of this Agreement is held invalid by a court of competent jurisdiction, such portion shall be deemed to be of no force and effect and the Agreement shall be construed as if such portion had not been included herein, provided however, if the deletion of such provision materially impairs the commercial value of this Agreement to either party, the parties shall attempt to renegotiate such provision in good faith.

10.4. ENTIRE AGREEMENT. This Agreement and all Exhibits attached hereto contain the sole and entire agreement and understanding of the parties hereto and their respective Affiliates and representatives related to the subject matter hereof and supersede all oral or written agreements concerning the subject matter made prior to the date of this Agreement.

10.5. AMENDMENT; WAIVER. This Agreement cannot be amended, changed, modified or supplemented orally, and no amendment, change, modification or supplement of this Agreement shall be recognized nor have any effect, unless the writing in which it is set forth is signed by Halsey and Watson, nor shall any waiver of any of the provisions of this Agreement be effective unless in writing and signed by the party to be charged therewith. The failure of either party to enforce, at any time, or for any period of time, any provision hereof or the failure of either party to exercise any option herein shall not be construed as a waiver of such provision or option and shall in no way affect that party's right to enforce such provision or exercise such option. No waiver of any provision hereof shall be deemed to be, or shall constitute, a waiver of any other provision, or with respect to any succeeding breach of the same provision.

10.6. GOVERNING LAW, DISPUTE RESOLUTION, ARBITRATION. This Agreement shall be governed by, and construed in accordance with, the laws of the State of California and the United States, as though made and to be fully performed therein without regard to conflicts of laws principles thereof.

The parties shall initially attempt in good faith to resolve any significant controversy, claim, allegation of breach or dispute arising out of or relating to this Agreement (hereinafter collectively

referred to as a "Dispute") through negotiations between senior executives of Watson and Halsey. If the Dispute is not resolved within thirty (30) days (or such other period of time mutually agreed upon by the parties) of notice of the Dispute (the "Executive Resolution Period"), then the parties agree to submit the Dispute to arbitration as provided herein. Unless otherwise mutually agreed by the parties, only if the Dispute is not resolved through negotiations as set forth herein, may a party resort to arbitration.

All Disputes relating in any way to this Agreement shall be resolved exclusively through arbitration conducted in accordance with the Commercial Arbitration Rule of the American Arbitration Association as then in effect. In the event either party demands arbitration, it shall do so within thirty (30) days after the expiration of the Executive Resolution Period (or any mutually agreed extension) and shall include a request that such arbitration be held within thirty (30) days of such demand. The arbitration hearing shall be held as soon as practicable. The arbitration hearing shall be held in Orange County, California and shall be before a single arbitrator selected by the parties in accordance with the Commercial Arbitration Rule of the American Arbitration Association pursuant to its rules on selection of arbitrators. The arbitrator shall render a formal, binding non-appealable resolution and award on each issue as expeditiously as possible but not more than ten (10) business days after the hearing. In any arbitration, the prevailing party shall be entitled to reimbursement of its reasonable attorneys fees and the parties shall use all reasonable efforts to keep arbitration costs to a minimum.

10.7. SINGULAR AND PLURAL FORMS. The use herein of the singular form shall also denote the plural form, and the use herein of the plural form shall denote the singular form, as in each case the context may require.

10.8. HEADINGS. The headings contained in this Agreement are for convenience of reference only and shall not constitute a part hereof or define, limit or otherwise affect the meaning of any of the terms or provisions hereof.

10.9. COUNTERPARTS. This Agreement may be executed in one or more counterparts, each of which shall be deemed an original, but all of which, when taken together, shall constitute one and the same instrument.

IN WITNESS WHEREOF, the parties have caused this Agreement to be executed by their respective duly authorized officers as of the date first above written.

WATSON PHARMACEUTICALS, INC.

By:/s/ Robert C. Funsten
Name:

Title: Senior Vice President

HALSEY DRUG CO., INC.

By:/s/ Michael Reicher
Name:

Title: Chief Executive Officer

SCHEDULE 1

Commercial Products

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