SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549
FORM 10-K
FOR ANNUAL AND TRANSITION REPORTS PURSUANT TO SECTION 13 OR 15(D)
OF THE SECURITIES EXCHANGE ACT OF 1934
(MARK ONE)

|X| ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934 FOR THE FISCAL YEAR ENDED DECEMBER 31, 1999

|_| TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934

FOR THE TRANSITION PERIOD FROM TO COMMISSION FILE NUMBER 1-10113

HALSEY DRUG CO., INC.
(EXACT NAME OF REGISTRANT AS SPECIFIED IN ITS CHARTER)

NEW YORK	11-0853640
(STATE OR OTHER JURISDICTION OF INCORPORATION OR ORGANIZATION)	(I.R.S. EMPLOYER IDENTIFICATION NO.)

695 NORTH PERRYVILLE ROAD, CRIMSON BUILDING NO. 2, ROCKFORD, ILLINOIS 61107
(ADDRESS OF PRINCIPAL EXECUTIVE OFFICES) (ZIP CODE)
REGISTRANT'S TELEPHONE NUMBER, INCLUDING AREA CODE: (815) 399-2060
SECURITIES REGISTERED PURSUANT TO SECTION 12(B) OF THE ACT:

TITLE OF EACH CLASS	NAME OF EACH EXCHANGE ON WHICH REGISTERED
COMMON STOCK, PAR VALUE $0.01	THE AMERICAN STOCK EXCHANGE

SECURITIES REGISTERED PURSUANT TO SECTION 12(G) OF THE ACT:
(TITLE OF CLASS)
NONE

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

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. |X|

As of March 31, 2000, the registrant had 14,427,619 shares of Common Stock, par value $0.01, outstanding. Based on the closing price of the Common Stock on March 31, 2000 ($1.875), the aggregate market value of the voting stock held by non-affiliates of the registrant was approximately $26,781,000.

DOCUMENTS INCORPORATED BY REFERENCE

Document	Where Incorporated
Proxy Statement for the 2000 Annual Meeting of Shareholders	Part III

CONTENTS

SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS

Certain statements in this Report under the captions Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations," Item 1, "Business", Item 3, "Legal Proceedings" and elsewhere in this Report constitute "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995 (the "Reform Act"). Such forward-looking statements involve known and unknown risks, uncertainties and other factors which may cause the actual results, performance or achievements of Halsey Drug Co., Inc. ("Halsey" or the "Company"), or industry results, to be materially different from any future results, performance, or achievements expressed or implied by such forward-looking statements. Such factors include, among others, the following: changes in general economic and business conditions; loss of market share through competition; introduction of competing products by other companies; the timing of regulatory approval and the introduction of new products by the Company; changes in industry capacity; pressure on prices from competition or from purchasers of the Company's products; regulatory changes in the generic pharmaceutical manufacturing industry; regulatory obstacles to the introduction of new products that are important to the Company's growth; availability of qualified personnel; the loss of any significant customers; and other factors both referenced and not referenced in this Report. When used in this Report, the words "estimate," "project," "anticipate," "expect," "intend," "believe," and similar expressions are intended to identify forward-looking statements.

PART I

ITEM 1. BUSINESS.

GENERAL

The Company, a New York corporation established in 1935, and its subsidiaries, are engaged in the manufacture, sale and distribution of generic drugs. A generic drug is the chemical and therapeutic equivalent of a brand-name drug for which patent protection has expired. A generic drug may only be manufactured and sold if patents (and any additional government-granted exclusivity periods) relating to the brand-name equivalent of the generic drug have expired. A generic drug is usually marketed under its generic chemical name or under a brand name developed by the generic manufacturer. The Company sells its generic drug products under its Halsey label and under private-label arrangements with drugstore chains and drug wholesalers. While subject to the same governmental standards for safety and efficacy as its brand-name equivalent, a generic drug is usually sold at a price substantially below that of its brand-name equivalent.

The Company manufactures its products at facilities in New York and Indiana. During the last several years, the Company has sought to diversify its businesses through strategic acquisitions and alliances and through the development, manufacture and sale of bulk chemical products used by others as raw materials in the manufacture of finished drug forms.

RECENT EVENTS

Regulatory Compliance

During the past several years, the Company's business has been adversely affected by the discovery of various manufacturing and record keeping problems identified with certain products manufactured at its Brooklyn, New York plant. In October 1991, the U.S. Food and Drug Administration (the "FDA") placed the Company on the FDA's Application Integrity Policy list and its restrictions (collectively, the "AIP"). Under the AIP, the FDA suspended all of the parent company's applications for new drug approvals, including Abbreviate New Drug Applications ("ANDAs") and Supplements to ANDAs. During the period that followed, the U.S. Department of Justice ("DOJ") conducted an investigation into the manufacturing and record keeping practices at the Company's Brooklyn plant. As a consequence, on June 21, 1993, the Company entered into a plea agreement (the "Plea Agreement") with the DOJ to resolve the DOJ's investigation. Under the terms of the Plea Agreement, the Company agreed to plead guilty to five counts of adulteration of a single drug product shipped in interstate commerce and related record keeping violations. The Plea Agreement also required the Company to pay a fine of $2,500,000 over five years in quarterly installments of $125,000 commencing in September 1993. As of February 28, 1998, the Company was in default of the payment terms of the Plea Agreement and had made payments aggregating $350,000. On March 27, 1998, the Company and the DOJ signed a Letter Agreement serving to amend the Plea Agreement relating to the terms of the Company's satisfaction of the fine assessed under the Plea Agreement. The Letter Agreement provides, among other things, that the Company will satisfy the remaining $2,150,000 of the fine through the payment of $25,000 on a monthly basis commencing June 1, 1998, plus interest on the outstanding balance. See "Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations--Liquidity and Capital Resources" for a more detailed description of the Letter Amendment to the Plea Agreement between the DOJ and the Company.

On June 29, 1993, the Company entered into a consent decree (the "Consent Decree") with the U.S. Attorney for the Eastern District of New York on behalf of the FDA that resulted from the FDA's investigation into the Brooklyn plant's compliance with the FDA's Current Good Manufacturing Practices ("CGMP") regulations. Under the terms of the Consent Decree, the Company was enjoined from shipping any solid dosage drug products (i.e., excluding liquid drug formulations) manufactured at the Brooklyn plant until the Company established, to the satisfaction of the FDA, that the methods used in, and the facilities and controls used for, manufacturing, processing, packing, labeling and holding any drug, were established, operated, and administered in conformity with the Federal Food, Drug, and Cosmetic Act and all CGMP Regulations. As part of satisfying these requirements, the Company was required to validate the manufacturing processes for each solid dosage drug product prior to manufacturing and shipping the drug product.

On October 23, 1996, the Company withdrew four of its ANDAs, including its ANDA (the "Capsules ANDA") for

acetaminophen/oxycodone capsules (the "Capsules"), and halted sales of the affected products. Net sales derived from the withdrawn Capsule ANDA were approximately $3 million and $8 million for the years ended December 31, 1996 and December 31, 1995, respectively, and accounted for approximately 24% and 40% of the Company's total net sales during such twelve month periods. The Company instituted the withdrawal of the Capsule ANDA at the suggestion of the FDA and in anticipation of its release from the AIP. At the FDA's suggestion, the Company retained outside consultants to perform validity assessments of its drug applications. Thereafter, in October 1996, the FDA recommended that several applications, including the Capsule ANDA, be withdrawn. As a basis for its decision, the FDA cited questionable and incomplete data submitted in connection with the applications. The FDA indicated that the withdrawal of the four ANDAs was necessary for the release of the Company from the AIP. The FDA further required submission by the Company of a Corrective Action Plan, which was prepared and submitted by the Company and accepted by the FDA.

On December 19, 1996, the FDA released the Company from the AIP. As a consequence, for the first time since October 1991, the Company was permitted to submit ANDAs to the FDA for review. Since its release from the AIP in December 1996, through the fiscal year ended December 31, 1999, the Company submitted 9 ANDAs for review by the FDA, including a new ANDA with respect to the Capsules. During the period from the Company's release from the AIP to March 31, 2000, the Company received the following ANDA approvals, all of which relate to ANDA filings made with the FDA subsequent to the Company's release from the AIP:

PRODUCT NAME (DRUG CLASS)	STRENGTH	TRADE NAME	STATUS
Hydrocodone Bitartate and Acetaminophen Tablets (narcotic analgesic)	5mg/500mg	Vicodin(R)(1)	FDA approval of ANDA received September 26, 1997.
Hydrocodone Bitartate and Acetaminophen Tablets (narcotic analgesic)	7.5mg/750mg	VicodinES(R)(1)	FDA approval of ANDA received September 26, 1997
Hydrocodone Bitartate and Acetaminophen Tablets, CIII (narcotic analgesic)	7.5mg/650mg	Lorcet Plus(R)(2)	FDA approval of ANDA received November 26, 1997.
Hydrocodone Bitartrate and Acetaminophen Tablets, CIII (narcotic analgesic)	10mg/650mg	Lorcet(R)(2)	FDA approval of ANDA received November 26, 1997.
Oxycodone HCI and Acetaminophen Capsules, CII (narcotic analgesic)	5mg/50mg	Tylox(R)(3)	FDA approval of ANDA received January 22, 1998.
Oxycodone HCI/Oxycodone Terephthalate Tablets, CII (narcotic analgesic)	4.5mg/325mm	Percodan(R)(4)	FDA approval of ANDA received July 24, 1998

Prednisolone Syrup, USP..... (systemic costicosteroid)	15mg/15ml	Prelone(R)(5)	FDA approval of ANDA received May 28, 1999
Hydrocodone Bitartrate and..... Homatropine Methylbromide Syrup (antitussive)	5 mg/1.5mg/5ml	Hydocan(R)(6)	FDA approval of ANDA received July 21, 1999

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(1) Registered trademark of Knoll Pharmaceutical Co.

(2) Registered trademark of Forest Laboratories, Inc.

(3) Registered trademark of McNeil Consumer Products Company

(4) Registered Trademark of DuPont Merck

(5) Registered Trademark of Muro Pharmaceuticals, Inc.

(6) Registered Trademark of Endo Pharmaceuticals, Inc.

During the fiscal year ended December 31, 1999, the Company submitted 1 ANDA for review by the FDA. The Company anticipates the submission during fiscal 2000 of 9 ANDA supplements or amendments. These supplements and amendments relate to the transfer of existing ANDAs from the Company's Brooklyn facility to its Congers facility as well as the transfer of certain ANDAs obtained from Barr Laboratories. Although the Company has been successful in receiving the ANDA approvals described above since its release from the AIP in December 1996, there can be no assurance that any of its newly submitted ANDAs, or supplements or amendments thereto or those contemplated to be submitted, will be approved by the FDA. The Company will not be permitted to market any new product unless and until the FDA approves the ANDA relating to such product. Failure to obtain FDA approval for the Company's pending ANDAs, or a significant delay in obtaining such approval, would adversely affect the Company's business operations and financial condition.

Strategic Alliance with Watson Pharmaceuticals

On March 29, 2000, the Company 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, for Watson's marketing and sale of the Company's core products and for Watson's extension of a $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 rights (the "Product") to Watson for aggregate consideration of $13,500,000 (the "Product Acquisition Agreement"). 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.

The Company and Watson also 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 completed 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 Agreement") 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, including, without limitation, the Product sold to Watson, 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 advance. 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. See "Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations" for a more detailed discussion of the $17,500,000 term loan from Watson.

Private Offering

On May 26, 1999, the Company consummated a private offering of securities for an aggregate purchase price of up to $22.8 million (the "Oracle offering"). The securities issued in the Oracle Offering consisted of five percent convertible senior secured debentures (the "1999 Debentures") and common stock purchase warrants (the "1999 Warrants"). The 1999 Debentures and 1999 Warrants were issued by the Company pursuant to a certain Debenture and Warrant Purchase Agreement dated May 26, 1999 (the "Oracle Purchase Agreement") by and among the Company, Oracle Strategic Partners, L.P. ("Oracle") and such other investors in the Company's March 10, 1998 offering electing to participate in the Oracle Offering (inclusive of Oracle, collectively, the "Oracle Investor Group").

The 1999 Debentures were issued at par and will become due and payable as to principle on March 15, 2003. Approximately $12.8 million in principle amount of the 1999 Debentures were issued on May 26, 1999. Interest on the principle amount of the 1999 Debentures, at the rate of 5% per annum, is payable on a quarterly basis.

The maximum principal amount of the 1999 Debentures are convertible into shares of the Company's common stock at a conversion price of $1.404 per share, for an aggregate of up to approximately 16,283,694 shares of the Company's common stock. The 1999 Warrants are exercisable for an aggregate of approximately 4,618,702 shares of the Company's common stock. Of such warrants, 2,309,351 warrants are exercisable at $1.404 per share and the remaining 2,309,351 warrants are exercisable at $2.279 per share. The 1999 Debentures and 1999 Warrants are convertible and exercisable, respectively, for an aggregate of approximately 20,902,396 shares of the Company's common stock.

Of the $22.8 million to be invested pursuant to the Oracle Purchase Agreement, $5,000,000 was funded by Oracle on May 26, 1999, the closing date of the Oracle Purchase Agreement, and an additional $5,000,000 was funded on July 27, 1999. On March 20, 2000, the Company and Oracle executed a Release Agreement releasing Oracle from its obligation to make the remaining investment of $5,000,000 pursuant to the Oracle Purchase Agreement. After giving effect to the Release Agreement with Oracle, the 1999 Debentures and 1999 Warrants are convertible and exercisable, respectively, for an aggregate of approximately 16,331,043 shares of the Company's common stock.

In addition to the $10,000,000 investment made by Oracle pursuant to the Oracle Purchase Agreement, approximately $7,037,000 of the 1999 Debentures issues pursuant to the Oracle Purchase Agreement were issued in exchange for the surrender of a like amount of principle and accrued interest outstanding under the Company's convertible promissory notes issued pursuant to various bridge loan transactions with Galen Partners, III, L.P., Galen Partners International, III, L.P., Galen Employee Fund, L.P. (collectively, "Galen Partners") and certain other investors, in the aggregate amount of $10,104,110 during the period from August, 1998 through and including May, 1999 (the "Galen Bridge Loans"). The remaining balance of the Galen Bridge Loans in the principal amount of $3,495,001 plus accrued and unpaid interest were satisfied with a portion of the proceeds of Oracle's second $5,000,000 installment on made July 27, 1999 pursuant to the Oracle Purchase Agreement.

Acquisition of Product ANDAs

On April 16, 1999, the Company completed an acquisition agreement with Barr Laboratories, Inc. ("Barr") providing for the Company's purchase of the rights to 50 pharmaceutical products (the "Barr Products"). Under the terms of the acquisition agreement with Barr, the Company acquired all of Barr's rights in the Barr Products, including all related governmental approvals (including ANDAs) and related technical data and information. In consideration for the acquisition of the Barr Products, the Company issued to Barr a common stock purchase warrant exercisable for 500,000 shares of the Company's common stock having an exercise price of $1.0625 per share (the fair market value of the Common Stock on the date of issuance) and having a term of five years. The acquisition agreement with Barr also allows Barr to purchase any of the Barr Products manufactured by the Company for a period of five years.

The Barr Products acquired by the Company were previously marketed by Barr, prior to its decision to strategically refocus its generic product portfolio several years ago. While the Barr Products cover a broad range of therapeutic applications and are the subject of approved ANDAs, the Company will be required to obtain approval from the U.S. Food and Drug Administration ("FDA") to permit manufacture and sale of any of the Barr Products, including site specific approval. The Company initially has identified 8 of the products for which it will devote substantial effort in seeking approval from the FDA for manufacture and sale. The Company estimates that certain of these Barr Product will be available for sale in the fourth quarter of 2000, although no assurance can be given that any of the Barr Products will receive FDA approval or that if approved, that the Company will be successful in the manufacture and sale of the such products. It is the Company's intention to continue to evaluate the remaining Barr Products on an ongoing basis to assess their prospects for commercialization and likelihood of obtaining regulatory approval.

Cessation and Relocation of Brooklyn, New York Operations

On March 22, 2000 the Company executed a Lease Termination and Settlement Agreement with the landlord of the Company's Brooklyn, New York manufacturing facility (the "Settlement Agreement"). The Settlement Agreement provides for the early termination of the lease covering the Brooklyn facility and provides the Company with the time necessary to transfer operations to the Company's Congers, New York facility and cease all manufacturing, research and development and warehouse operations currently conducted in Brooklyn. The Settlement Agreement provides for the termination of the Brooklyn facility lease on August 31, 2000, subject to the Company's right to extend the term to March 31, 2001. The original lease provided for a term expiring December 31, 2005 with a rental payment obligation of $6,715,000 during the period from September 1, 2000 through December 31, 2005.

The Settlement Agreement provided for the Company's payment of a termination fee of $1,150,000, the advance payment of rent through August 31, 2000 and the deposit of a restoration escrow of $200,000 to be used for facility repairs. The Company also deposited $390,600 in escrow with its counsel. This escrow amount represents the rental payments for the period September 1, 2000 through March 31, 2001 and will be returned to the Company in the event it vacates the

Brooklyn facility on or prior to August 31, 2000. The Company recorded a total charge against earnings of approximately $3,220,000 resulting from the elimination of its Brooklyn, New York operations. See "Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations" for a more detailed discussion of this charge against earnings.

Lease of Congers, New York Facility

Effective March 22, 1999, the Company leased, as sole tenant, a pharmaceutical manufacturing facility located in Congers, New York (the "Congers Facility") from Par Pharmaceuticals, Inc. ("Par") pursuant to an Agreement to Lease (the "Lease"). The Congers Facility contains office, warehouse and manufacturing space and is approximately 35,000 square feet. The Lease provides for a term of three years, with a two year renewal option and provides for annual fixed rent of $500,000 per year during the primary term of the Lease and $600,000 per year during the option period. The Lease also covers certain manufacturing and related equipment previously used by Par in its operations at the Congers Facility (the "Leased Equipment"). In connection with the execution of the Lease, the Company and Par entered into a certain Option Agreement pursuant to which the Company may purchase the Congers Facility and the Lease Equipment at any time during the lease term for $5 million.

As part of the execution of the Lease, the Company and Par entered into a certain Manufacturing and Supply Agreement (the "M&S Agreement") having a minimum term of twenty seven months. The M&S Agreement provides for the Company's contract manufacture of certain designated products manufactured by Par at the Congers Facility prior to the effective date of the Lease. The M&S Agreement also provides that Par will purchase a minimum of $1,150,000 in product during the initial 18 months of the Agreement. The M&S Agreement further provides that the Company will not manufacture, supply, develop or distribute the designated products to be supplied by the Company to Par under the M&S Agreement to or for any other person for a period of three years.

PRODUCTS AND PRODUCT DEVELOPMENT

Generic Drug Products

The Company historically has manufactured and sold a broad range of prescription and over-the-counter drug products. The Company's pharmaceutical product list currently includes a total of approximately 31 products, consisting of 21 dosage forms and strengths of prescription drugs and 10 dosage forms and strengths of over-the-counter drugs. Each dosage form and strength of a particular drug is considered in the industry to be a separate drug product. The Company's drug products are sold in various forms, including liquid and powder preparations, compressed tablets and two-piece, hard-shelled capsules.

Most of the generic drug products manufactured by the Company can be classified within one of the following categories:

1. Antibiotics,

2. Narcotic analgesics,

3. Anti-infective and anti-tubercular drugs,

4. Antihistamines and antihistaminic decongestants,

5. Antitussives, or

6. Steroids

During fiscal 1999, sales of antibiotics and narcotic analgesics accounted for approximately 67% of total net sales during such year. The Company anticipates that sales of antibiotics and narcotic analgesics will continue to represent a significant portion of the Company's revenue.

The Company's development strategy for new drug products has been to focus on the development of a broad-range of generic form drugs, each of which (i) has developed a solid market acceptance with a wide base of customers, (ii) can be sold on a profitable basis notwithstanding intense competition from other drug manufacturers, and (iii) is no longer under patent protection. The Company has also diversified its current product line to include some less widely prescribed drugs as to which limited competition might be expected. While the Company will continue the development of its finished goods pharmaceutical business, including the rehabilitation of the product ANDAs acquired from Barr, the Company's will dedicate increasing resources to the expansion and enhancement of its operations devoted to the development and manufacture of APIs for use in the Company's finished dosage products as well as for sale to third party pharmaceutical companies, including Watson, in the form and API and finished dosage products.

Development activities for each new generic drug product begin several years in advance of the patent expiration date of the brand-name drug equivalent. This is because the profitability of a new generic drug usually depends on the ability of the Company to obtain FDA approval to market that drug product upon or immediately after the patent expiration date of the equivalent brand-name drug. Being among the first to market a new generic drug product is vital to the profitability of the product. As other off-patent drug manufacturers receive FDA approvals on competing generic products, prices and revenues typically decline. Accordingly, the Company's ability to attain profitable operations will, in large part, depend on its ability to develop and introduce new products, the timing of receipt of FDA approval of such products and the number and timing of FDA approvals for competing products.

Active Pharmaceutical Ingredients

In the last few years, the Company has increased its efforts to develop and manufacture APIs, also known as bulk chemical products. The development and sale of APIs generally is not subject to the same level of regulation as is the development and sale of drug products. Accordingly, APIs may be brought to market substantially sooner than drug products. As described under the caption "Recent Events - Strategic Alliance with Watson Pharmaceuticals" above, the Company is a party to agreements with Watson Pharmaceuticals providing for Watson's right to negotiate for a supply of select APIs currently in development and to be developed by the Company. In addition to its alliance with Watson, it is the Company's intention to develop APIs for its own manufacture and sale (both in API and finished dosage form) and in partnership with other pharmaceutical manufacturers. A significant portion of the net proceeds from the Watson loan transaction described above will be devoted to the upgrade of its Culver, Indiana manufacturing facility operated by its Houba subsidiary, including HVAC, equipment and operational upgrades. During fiscal 1999, all of the Company's revenues were delivered from the sale of finished dosage products. It is the Company's expectation that in connection with a strategic alliance with Watson and other API development efforts, in addition to assisting in the expansion of the Company's line of finished products, the Company will generate revenues from the sale of APIs starting in the latter part of 2000 and such revenue segment will likely increase thereafter as a percentage of total revenue.

RESEARCH AND DEVELOPMENT

The Company currently conducts research and development activities at each of its Brooklyn and Indiana facilities. Once the cessation and relocation of the Company's Brooklyn, New York operations are completed, the Company's research and development activities previously conducted in Brooklyn will be transferred to its Congers, New York facility. The Company's research and development activities consist primarily of new generic drug product development efforts and manufacturing process improvements, the development for sale of new chemical products and the development of APIs. New drug product development activities are primarily directed at conducting research studies to develop generic drug formulations, reviewing and testing such formulations for therapeutic equivalence to brand name products and additional testing in areas such as bioavailability, bioequivalence and shelf-life. For fiscal years 1999, 1998 and 1997, total research and development expenditures were $1,075,000, $651,000 and $979,000, respectively. During 2000, the Company's research and development efforts will cover finished dosage products and APIs in a variety of therapeutic applications.

As of March 31, 2000, the Company maintained a full-time staff of 11 in its Research and Development Departments.

MARKETING AND CUSTOMERS

The application of the AIP to the Company's operations until December 1996, combined with the Company's continuing operating losses and lack of adequate working capital during fiscal 1997 and the first quarter of 1998 resulted in the Company's inability to maintain sufficient raw materials and finish goods inventories to permit the Company to actively solicit customer orders, and when orders were received, to fill such orders promptly. Following the completion in March 1998 of the offering with Galen Partners (the "Galen Offering"), new Management adopted a marketing strategy focused on developing and maintaining sufficient raw materials and finish goods inventories so as to permit a targeted sales effort by the Company to a core customer group, with an emphasis on quality, prompt product delivery and excellent customer service.

The strategic alliance with Watson entered into on March 29, 2000 provides for the Company's core products portfolio to be sold by Watson's sales force under Watson's label. Accordingly, the Company intends to discontinue sales efforts of these products. The two companies are working together during the second quarter of 2000 to effect an orderly transition of existing sales agreements and orders from Halsey to Watson. The Company continues to perform limited contract manufacturing of certain non-core products for other pharmaceutical companies.

During 1999, the Company had net sales to two customers aggregating approximately 25.3% of total sales. The Company believes that the loss of these customers would have a material adverse effect on the Company. During 1998 the Company had net sales to two customers, aggregating 19.1% of total sales. During 1997, the Company had net sales to one customer in excess of 10% of total sales, aggregating 22.3% of total sales.

The estimated dollar amount of the backlog of orders for future delivery as of March 31, 2000 was approximately $800,000 as compared with approximately $500,000 as of March 15, 1999. Although these orders are subject to cancellation, management expects to fill substantially all orders by the second quarter of 2000. The increase in the Company's backlog as of March 31, 2000 compared to that in 1999 is largely a function of an increase in market penetration.

GOVERNMENT REGULATION

General

All pharmaceutical manufacturers, including the Company, are subject to extensive regulation by the Federal government, principally by the FDA, and, to a lesser extent, by state and local governments. Additionally, the Company is subject to extensive regulation by the U.S. Drug Enforcement Agency ("DEA") as a manufacturer of controlled substances. The Company cannot predict the extent to which it may be affected by legislative and other regulatory developments concerning its products and the healthcare industry generally. The Federal Food, Drug, and Cosmetic Act, the Generic Drug Enforcement Act of 1992, the Controlled Substance Act and other Federal statutes and regulations govern or influence the testing, manufacture, safe labeling, storage, record keeping, approval, pricing, advertising, promotion, sale and distribution of pharmaceutical products. Noncompliance with applicable requirements can result in fines, recall or seizure of products, criminal proceedings, total or partial suspension of production, and refusal of the government to enter into supply contracts or to approve new drug applications. The FDA also has the authority to revoke approvals of new drug applications. The ANDA drug development and approval process now averages approximately eight months to two years. The approval procedures are generally costly and time consuming.

FDA approval is required before any "new drug," whether prescription or over-the-counter, can be marketed. A "new drug" is one not generally recognized by qualified experts as safe and effective for its intended use. Such general recognition must be based on published adequate and well controlled clinical investigations. No "new drug" may be introduced into commerce without FDA approval. A drug which is the "generic" equivalent of a previously approved prescription drug also will require FDA approval. Furthermore, each dosage form of a specific generic drug product requires separate approval by the FDA. In general, as discussed below, less costly and time consuming approval procedures may be used for generic equivalents as compared to the innovative products. Among the requirements for drug approval is that the prospective manufacturer's methods must conform to the CGMPs. CGMPs apply to the manufacture, receiving, holding and shipping of all drugs, whether or not approved by the FDA. CGMPs must be followed at all times during which the drug is manufactured. To ensure full compliance with standards, some of which are set forth in regulations, the Company must continue to expend time, money and effort in the areas of production and quality control. Failure to so comply risks delays in approval of drugs, disqualification from eligibility to sell to the government, and possible FDA enforcement actions, such as an injunction against shipment of the Company's products, the seizure of noncomplying drug products, and/or, in serious

cases, criminal prosecution. The Company's manufacturing facilities are subject to periodic inspection by the FDA.

In addition to the regulatory approval process, the Company is subject to regulation under Federal, state and local laws, including requirements regarding occupational safety, laboratory practices, environmental protection and hazardous substance control, and may be subject to other present and future local, state, Federal and foreign regulations, including possible future regulations of the pharmaceutical industry.

Drug Approvals

There are currently three ways to obtain FDA approval of a new drug.

1. New Drug Applications ("NDA"). Unless one of the procedures discussed in paragraph 2 or 3 below is available, a prospective manufacturer must conduct and submit to the FDA complete clinical studies to prove a drug's safety and efficacy, in addition to the bioavailability and/or bioequivalence studies discussed below, and must also submit to the FDA information about manufacturing practices, the chemical make-up of the drug and labeling.

2. Abbreviated New Drug Applications ("ANDA"). The Drug Price Competition and Patent Term Restoration Act of 1984 (the "1984 Act") established the ANDA procedure for obtaining FDA approval for those drugs that are off-patent or whose exclusivity has expired and that are bioequivalent to brand-name drugs. An ANDA is similar to an NDA, except that the FDA waives the requirement of conducting complete clinical studies of safety and efficacy, although it may require expanded clinical bioavailability and/or bioequivalence studies. "Bioavailability" means the rate of absorption and levels of concentration of a drug in the blood stream needed to produce a therapeutic effect. "Bioequivalence" means equivalence in bioavailability between two drug products. In general, an ANDA will be approved only upon a showing that the generic drug covered by the ANDA is bioequivalent to the previously approved version of the drug, i.e., that the rate of absorption and the levels of concentration of a generic drug in the body are substantially equivalent to those of a previously approved equivalent drug. The principle advantage of this approval mechanism is that an ANDA applicant is not required to conduct the same preclinical and clinical studies to demonstrate that the product is safe and effective for its intended use.

The 1984 Act, in addition to establishing the ANDA procedure, created new statutory protections for approved brand-name drugs. In general, under the 1984 Act, approval of an ANDA for a generic drug may not be made effective until all product and use patents listed with the FDA for the equivalent brand name drug have expired or have been determined to be invalid or unenforceable. The only exceptions are situations in which the ANDA applicant successfully challenges the validity or absence of infringement of the patent and either the patent holder does not file suit or litigation extends more than 30 months after notice of the challenge was received by the patent holder. Prior to enactment of the 1984 Act, the FDA gave no consideration to the patent status of a previously approved drug. Additionally, under the 1984 Act, if specific criteria are met, the term of a product or use patent covering a drug may be extended up to five years to compensate the patent holder for the reduction of the effective market life of that patent due to federal regulatory review. With respect to certain drugs not covered by patents, the 1984 Act sets specified time periods of two to ten years during which approvals of ANDAs for generic drugs cannot become effective or, under certain circumstances, ANDAs cannot be filed if the equivalent brand-name drug was approved after December 31, 1981.

3. "Paper" NDA. An alternative NDA procedure is provided by the 1984 Act whereby the applicant may rely on published literature and more limited testing requirements. While that alternative sometimes provides advantages over the ANDA procedure, it is not frequently used.

Generic Drug Enforcement Act

As a result of hearings and investigations concerning the activities of the generic drug industry and the FDA's generic drug approval process, Congress enacted the Generic Drug Enforcement Act of 1992 (the "Generic Drug Act"). The Generic Drug Act confers significant new authority upon the FDA to impose debarment and civil penalties for individuals and companies who commit certain illegal acts relating to the generic drug approval process.

The Generic Drug Act requires the mandatory debarment of companies or individuals convicted of a federal felony for conduct relating to the development or approval of any ANDA, and gives the FDA discretion to debar corporations or

individuals for similar conduct resulting in a federal misdemeanor or state felony conviction. The FDA may not accept or review during the period of debarment (one to ten years in the case of mandatory, or up to five years in the case of permissive, debarment of a corporation) any ANDA submitted by or with the assistance of the debarred corporation or individual. The Generic Drug Act also provides for temporary denial of approval of generic drug applications during the investigation of crimes that could lead to debarment. In addition, in more limited circumstances, the Generic Drug Act provides for suspension of the marketing of drugs under approved generic drug applications sponsored by affected companies. The Generic Drug Act also provides for fines and confers authority on the FDA to withdraw, under certain circumstances, approval of a previously granted ANDA if the FDA finds that the ANDA was obtained through false or misleading statements. The Company was not debarred as a result of the FDA investigation and settlement and the Consent Decree with the FDA makes no provision therefor.

Healthcare Reform

Several legislative proposals to address the rising costs of healthcare have been introduced in Congress and several state legislatures. Many of such proposals include various insurance market reforms, the requirement that businesses provide health insurance coverage for all their employees, significant reductions in the growth of future Medicare and Medicaid expenditures, and stringent government cost controls that would directly control insurance premiums and indirectly affect the fees of hospitals, physicians and other healthcare providers. Such proposals could adversely affect the Company's business by, among other things, reducing the demand, and the prices paid, for pharmaceutical products such as those produced and marketed by the Company. Additionally, other developments, such as (i) the adoption of a nationalized health insurance system or a single payor system, (ii) changes in needs-based medical assistance programs, or (iii) greater prevalence of capitated reimbursement of healthcare providers, could adversely affect the demand for the Company's products.

COMPETITION

The Company competes in varying degrees with numerous companies in the health care industry, including other manufacturers of generic drugs (among which are divisions of several major pharmaceutical companies) and manufacturers of brand-name drugs. Many of the Company's competitors have substantially greater financial and other resources and are able to expend more money and effort than the Company in areas such as marketing and product development. Although a company with greater resources will not necessarily receive FDA approval for a particular generic drug before its smaller competitors, relatively large research and development expenditures enable a company to support many FDA applications simultaneously, thereby improving the likelihood of being among the first to obtain approval of at least some generic drugs.

One of the principal competitive factors in the generic pharmaceutical market is the ability to introduce generic versions of brand-name drugs promptly after a patent expires. The Company believes that it was at a competitive disadvantage until its release from the AIP program and the FDA's resumption of review of ANDAs submitted by the Company's Brooklyn plant. See "Government Regulation--Generic Drug Enforcement Act" above. Other competitive factors in the generic pharmaceutical market are price, quality and customer service (including maintenance of sufficient inventories for timely deliveries).

RAW MATERIALS

The raw materials essential to the Company's business are bulk pharmaceutical chemicals purchased from numerous sources. Raw materials are generally available from several sources. The Federal drug application process requires specification of raw material suppliers. If raw materials from a supplier specified in a drug application were to become unavailable on commercially acceptable terms, FDA supplemental approval of a new supplier would be required. During 1999 and 1998, the Company purchased approximately $1,107,000 and $2,583,000, respectively, of its raw materials (constituting 15% and 29%, respectively, of its aggregate purchases of raw materials) from Mallinckrodt. Although the Company is now able to submit supplements to the FDA in order to allow the Company to purchase raw materials from alternate sources, there can be no assurance that if the Company were unable to continue to purchase raw materials from this supplier, that the Company would be successful in receiving FDA approval to such supplement or that it would not face difficulties in obtaining raw materials on commercially acceptable terms. Failure to receive FDA approval for, and to locate, an acceptable alternative source of raw materials would have a material adverse effect on the Company.

The DEA limits the quantity of the Company's inventories of certain raw materials used in the production of controlled substances based on historical sales data. In view of the Company's recently depressed sales volume, these DEA limitations could increase the likelihood of raw material shortages and of manufacturing delays in the event the Company experiences increased sales volume or is required to find new suppliers of these raw materials.

SUBSIDIARIES

The Company's Indiana manufacturing operations are conducted by Houba, Inc., an Indiana corporation and wholly-owned subsidiary of the Company. Halsey Pharmaceuticals, Inc., a Delaware corporation, is a wholly-owned subsidiary which is currently inactive. The Company also has the following additional subsidiaries, each of which is currently inactive and anticipated to be dissolved during the remainder of the 2000 fiscal year: Indiana Fine Chemicals Corporation, a Delaware corporation, H.R. Cenci Laboratories, Inc., a California corporation, Cenci Powder Products, Inc., a Delaware corporation, Blue Cross Products, Inc., a New York corporation, and The Medi-Gum Corporation, a Delaware corporation.

EMPLOYEES

As of March 31, 2000, the Company had approximately 179 full-time employees. Approximately 39 employees are administrative and professional personnel and the balance are in production and shipping. Among the professional personnel, 11 are engaged in research and product development. Approximately 46 employees at the Company's Brooklyn facility are represented by a local collective bargaining unit. The collective bargaining agreement between the Company and the union was extended on March 5, 1998 (retroactive to July 2, 1997) and expires June 30, 2000. As discussed above under the caption "Recent Events - Cessation and Relocation of Brooklyn, New York Operations", the Company is in the process of ceasing operations at its leased facility in Brooklyn, New York. The Company estimates that it will complete its relocation of the operations conducted in Brooklyn to its Congers, New York facility by August 31, 2000. After giving effect to the cessation of operations in Brooklyn, New York, the Company estimates that it will have approximately 107 employees. Management believes that its relations with its employees are satisfactory.

ITEM 2. PROPERTIES.

Halsey leases, as sole tenant, a pharmaceutical manufacturing facility of approximately 35,000 square feet located at 77 Brenner Drive, Congers, New York. The Agreement of Lease, with an unaffiliated third party, contains a three year term with a two year renewal option and provides for annual fixed rent of $500,000 per year during the primary term of the Lease and $600,000 per year during the renewal period. The primary term of the Lease expires on March 21, 2002. The Leased facility houses a portion of the Company's manufacturing operations and includes office and warehouse space. The Lease also contains an option pursuant to which the Company may purchase the leased premises and improvements (including certain production and related equipment) for a purchase price of $5 million, exercisable at any time during the Lease term.

Halsey leases, as sole tenant, a total of approximately 147,000 square feet in three buildings on Pacific Street and Dean Street in Brooklyn, New York. Each of these leases is between Halsey and unaffiliated lessors. The approximate aggregate minimum rental commitments under these operating leases are as follows: $1,023,000 for the year 1999 and $781,000 for the year 2000. The leases of the Brooklyn, New York facility expire on August 31, 2000, subject to the Company's right to extend the lease term to March 31, 2001. The Company is in the process of ceasing and relocating its Brooklyn operations to its Congers, New York facility. See "Item 1. Business - Recent Events - Cessation and Relocation of Brooklyn, New York Operations."

Halsey leases approximately 4,700 square feet of office space located at 695 North Perryville Road, Building No. 2, Rockford, Illinois. The lease is between the Company and an unaffiliated lessor. The lease has a term of two years expiring August 31, 2000 and calls for annual rental, including maintenance and common area expense, of approximately $50,000 per year. The Company is currently in discussion with the landlord to extend the term of the lease of this facility. This leased facility houses the Company's principal executive offices, including its sales, administration and finance operations.

The Company's Houba, Inc. subsidiary owns approximately 45,000 square feet of building space on approximately 30 acres of land in Culver, Indiana, which includes a 15,000 square foot manufacturing facility. This manufacturing facility

houses separate plants for the production of certain raw materials, capsules and tablets. In 1996, in conjunction with a settlement with two former employees, the Company acquired real property, improved by a residential property, in Culver, Indiana adjacent to the manufacturing facility.

ITEM 3. LEGAL PROCEEDINGS.

GOVERNMENTAL PROCEEDINGS

Reference is also made to the discussion of the Company's Plea Agreement and Letter Agreement with the DOJ contained in "Item 1. Business--Recent Events" and "Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations."

OTHER LEGAL PROCEEDINGS

Beginning in 1992, actions were commenced against the Company and numerous other pharmaceutical manufacturers in the Pennsylvania Court of Common Pleas, Philadelphia Division, in connection with the alleged exposure to diethylstilbestrol ("DES"). The defense of all of such matters was assumed by the Company's insurance carrier, and a substantial number have been settled by the carrier. Currently, several actions remain pending with the Company as a defendant, and the insurance carrier is defending each action. Similar actions were brought in Ohio, and have been dismissed based on Ohio law. The Company does not believe any of such actions will have a material impact on the Company's financial condition.

The Company has been named as a defendant in one additional action which has been referred to the Company's insurance carrier and has been accepted for defense. The action, Alonzo v. Halsey Drug Co., Inc. and K-Mart Corp., No. 64DOT-95111-CT-2736 (Indiana Superior Court, Porter County), was commenced on November 7, 1995 and involves a claim for unspecified damages relating to the alleged ingestion of "Doxycycline 100." The Company does not believe this action will have a material impact on the Company's financial condition.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS.

No matters were submitted to a vote of security holders during the fourth quarter of 1999.

PART II

ITEM 5. MARKET PRICE FOR THE REGISTRANT'S COMMON EQUITY AND RELATED SECURITY HOLDER MATTERS.

MARKET AND MARKET PRICES OF COMMON STOCK

The Company's Common Stock is listed on the American Stock Exchange (the "Exchange") under the symbol "HDG." Set forth below for the periods indicated are the high and low sales prices for the Common Stock as reported on the Exchange.

PERIOD	HIGH	LOW
2000 Fiscal Year		
First Quarter (through March 31, 2000)	2 3/8	1
1999 Fiscal Year		
First Quarter	1 9/16	1
Second Quarter	3 3/16	1
Third Quarter	3 1/8	2
Fourth Quarter	2 3/4	3/4
1998 Fiscal Year		
First Quarter	3 5/8	1 1/4
Second Quarter	3 1/8	2 3/8
Third Quarter	2 3/4	1 1/2
Fourth Quarter	1 7/8	1

The Company does not meet certain of the Exchange's criteria for continued listing. The Company was informed by the Exchange that it has determined to delist the Company's Common Stock as it does not meet the Exchange's criteria for continued listing. Such criteria include minimum levels of shareholders equity and the absence of years of net losses from continuing operations. The Company has exercised its right to appeal the Exchange's decision. There can be no assurance that the Company's common stock will remain listed on the Exchange. If the Common Stock should become delisted from the Exchange, trading, if any, in the Common Stock would continue on the OTC Bulletin Board, an NASD-sponsored inter-dealer quotation system, or in what is commonly referred to as the "Pink Sheets". In such event, a shareholder may find it more difficult to dispose of, or to obtain accurate quotations as to the market value of the Common Stock.

HOLDERS

There were 788 holders of record of the Company's common stock on March 31, 2000. This number, however, does not reflect the ultimate number of beneficial holders of the Company's common stock.

DIVIDEND POLICY

The payment of cash dividends from current earnings is subject to the discretion of the Board of Directors and is dependent upon many factors, including the Company's earnings, its capital needs and its general financial condition. The terms of the Company's 5% convertible senior secured debentures and the Term Loan Agreement with Watson Pharmaceuticals prohibit the Company from paying cash dividends. The Company does not intend to pay any cash dividends in the foreseeable future.

PRIVATE OFFERINGS

The Company secured bridge financing from Galen in the aggregate amount of approximately $1,500,000, funded through two separate bridge loan transactions in December, 1999 (collectively, the "Bridge Loans"). In consideration for the extension for the Bridge Loans, the Company issued common stock purchase warrants to purchase an aggregate of 75,000

shares of the Company's Common Stock having an exercise price equal to the fair market value of the Common Stock at the date of issuance.

Each of the lenders in the Bridge Loans are accredited investors as defined in Rule 501(a) of Regulation D promulgated under the Securities Act of 1933, as amended (the "Act"). The warrants issued in connection with the Bridge Loans were issued without registration under the Act in reliance upon Section 4(2) of the Act and Regulation D promulgated thereunder.

ITEM 6. SELECTED FINANCIAL DATA.

The selected consolidated financial data presented on the following pages for the years ended December 31, 1999, 1998, 1997, 1996 and 1995 are derived from the Company's audited Consolidated Financial Statements. The Consolidated Financial Statements as of December 31, 1999 and December 31, 1998, and for each of the years in the three year period ended December 31, 1999, and the report thereon, are included elsewhere herein. The selected financial information as of and for the years ended December 31, 1997, 1996 and 1995 are derived from the audited Consolidated Financial Statements of the Company not presented herein.

The information set forth below is qualified by reference to, and should be read in conjunction with, the Consolidated Financial Statements and related notes thereto included elsewhere in this Report and "Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations."

	YEARS ENDED DECEMBER 31,				
	1999	1998	1997	1996	1995
	(IN THOUSANDS, EXCEPT PER SHARE DATA)				
OPERATING DATA:					
Net sales	$ 11,420	$ 8,841	$ 9,088	$ 12,379	$ 20,225
Costs and expenses					
Cost of sales	15,316	12,712	15,407	16,826	18,097
Research and development	1,075	651	979	1,854	818
Selling, general and administrative	7,383	8,078	6,308	7,486	6,098
Plant shutdown costs	3,220	--	--	--	--
Interest expense	2,851	1,285	1,144	1,708	1,307
Amortization of deferred debt discount and private offering cost	1,825	661			
Other (income) expense	(187)	(1,822)	264	(1,000)	(2,288)
Income (loss) before provision for income taxes	(20,063)	(12,724)	(15,014)	(14,495)	(3,807)
Provision (benefit) for income taxes	--	--	--	--	296
Net income (loss)	$ (20,063)	$ (12,724)	$ (15,014)	$ (14,495)	$ (4,103)
Net income (loss) per share	$ (1.40)	$ (.92)	$ (1.12)	$ (1.49)	$ (.52)
Weighted average common shares outstanding	14,325,551	13,812,529	13,434,215	9,724,106	7,886,101

	DECEMBER 31,				
	1999	1998	1997	1996	1995
	(IN THOUSANDS, EXCEPT PER SHARE DATA)				
BALANCE SHEET DATA:					
Working capital (deficiency)	$ (5,181)	$ (6,665)	$(22,304)	$(12,201)	$ (7,393)
Total assets	12,495	16,413	7,667	11,982	18,862
Total liabilities	54,869	45,366	27,524	19,063	20,402
Retained earnings (accumulated deficit)	(77,284)	(57,221)	(44,497)	(29,484)	(14,989)
Stockholders' equity (deficit)	(42,374)	(28,953)	(19,857)	(7,081)	(1,540)

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS.

Certain statements set forth under this caption constitute "forward-looking statements" within the meaning of the Reform Act. See "Special Note Regarding Forward-Looking Statements " on page 1 of this Report for additional factors relating to such Statements.

OVERVIEW

The Company reported a net loss of $20,063,000 or $1.40 per share for the year ended December 31, 1999 as compared with the net loss of $12,724,000 or $ .92 per share for 1998. Included in the loss for 1999 is a one-time charge of $3,220,000 resulting from the Company's decision to shutdown its Brooklyn operation. Net Sales for the year ended December 31, 1999 were approximately $11,420,000 as compared to net sales of approximately $8,841,000 for 1998. Notwithstanding these results, the Company had the following achievements in 1999:

- - Obtained a state-of-the-art pharmaceutical facility by leasing a 35,000 square foot facility in Congers, NY.

- - Acquired rights to over 50 products from Barr Laboratories. Certain of these products will be systematically updated and introduced to the market over the next three years.

- - Received approval from the FDA of two ANDA's and submitted one other for approval.

- - Subsequent to year end, the Company completed various strategic alliance transactions with Watson Pharmaceuticals, Inc.

RESULTS OF OPERATIONS

The following chart reflects expenses, earnings, income, losses and profits expressed as a percentage of net sales for the years 1999, 1998 and 1997.

	PERCENTAGE OF NET SALES YEAR ENDED DECEMBER			PERCENTAGE CHANGE YEAR-TO-YEAR INCREASE (DECREASE) YEARS ENDED DECEMBER 31,	
	1999	1998	1997	1998 TO 1999	1997 TO 1998
Net sales	100%	100%	100%	29.2	(2.7)
Cost of Goods	134.1	143.8	169.5	20.5	(17.5)
Gross Profit	(34.1)	(43.8)	(69.5)	.6	(38.7)
Research & Development	9.4	7.4	10.8	65.1	(33.5)
Selling, general and administrative expense	64.6	91.4	69.4	(8.6)	29.5
Plant shutdown costs	28.2	--	--	--	--
(Loss) from operations	(136.4)	(142.5)	(149.7)	23.6	(6.7)
Interest expense	25.0	14.5	12.6	121.9	70.1
Amortization of deferred debt discount and private offering cost	16.0	7.5	--	176.1	--
Other (income) expenses	(1.6)	(20.6)	2.9	(89.7)	--
(Loss) before income taxes	(175.7)	(143.9)	(165.2)	57.7	(14.6)
Net (loss)	(175.7)%	(143.9)%	(165.2)%	57.7%	(14.6)%

NET SALES

Net sales for 1999 of $11,420,000 represents an increase of $2,579,000 as compared to net sales for 1998. The increase is attributable to greater market penetration as well as the introduction of additional products, primarily prednisolone, which accounted for approximately $815,000 of new sales.

Net sales for 1998 of $8,841,000 represents a decrease of $247,000 as compared to net sales for 1997. The decrease is attributable in part to a reduction in toll manufacturing revenue from Mallinckrodt of approximately $878,000 from the prior year. Additionally, the Company was unable to market successfully to the retail pharmacy marketplace until the third quarter of 1998 because during fiscal 1996 and 1997, the Company had failed to pay required rebates to state Medicaid agencies. This caused those states to deny medicaid reimbursement to the retail pharmacies on their sales of the Company's products. Commensurate with the infusion of new capital and management in March, 1998, the Company began reestablishing itself in good standing with all states. In April 1998, the Company entered into a new contract with the Health Care Finance Authority ("HCFA") and paid outstanding rebates due to various states. The states completed the reinstatement of the Company on their medicaid reimbursement by July, 1998. The Company has been in good standing with HCFA and the individual states since July 1998 and expects this past non-compliance will have no impact on future results of operations or liquidity. Also during much of 1998, the Company experienced difficulty in obtaining certain raw materials which reduced sales. These shortages were remedied by December 31, 1998.

GROSS MARGINS

The Company's gross margin for 1999 improved to (34.1)% versus (43.8)% for 1998. The improvement in 1999 is due primarily to the leveraging effect of greater sales over certain fixed manufacturing expenses.

The Company's gross margin for 1998 of (43.8)% is a 38.7% improvement over gross margin for 1997. This improvement is due, in part, to the elimination of non-core manufacturing operations in California, tighter inventory controls and a general reduction in manufacturing labor. Additionally, the Company's revenues in 1998 from sales to Mallinckrodt under a toll manufacturing agreement decreased by approximately $878,000. The gross margins on these products were substantially less than on the Company's other products.

RESEARCH & DEVELOPMENT EXPENSES

For 1999, research and development expenses amounted to $1,075,000 as compared to $651,000 for 1998. The increase primarily reflects the costs of additional regulatory personnel hired during 1999 to perform work in conjunction with new product development and the transfer of certain Barr ANDAs acquired during 1999.

For 1998, research and development expenses amounted to $651,000 as compared to $979,000 for 1997. The decrease primarily reflects the costs of biostudies performed in 1997 that were not duplicated in 1998.

The Company expects research and development expenses to increase significantly in 2000 consistent with its plans to increase the number of Barr ANDA's transferred as compared to 1999 and to develop additional active pharmaceutical ingredients at its Culver, Indiana facility.

SELLING, GENERAL AND ADMINISTRATIVE EXPENSES

Selling, general and administrative costs were $7,383,000 (64.6% of net sales) for 1999 compared to $8,078,000 (91.4% of net sales) for 1998. This decrease is primarily due to the reduced legal expenses in 1999 as compared to 1998.

Selling, general and administrative costs were $8,078,000 (91.4% of net sales) for 1998 compared to $6,308,000 (69.4% of net sales) for 1997. This increase is primarily due to costs associated with legal expenses and settlement costs of certain litigation ($550,000), severance costs associated with personnel reductions ($250,000), installation of a new information system ($100,000) and costs associated with expanded regulatory and compliance departments ($300,000).

PLANT SHUTDOWN COSTS

In the fourth quarter of 1999, the Company decided to discontinue its Brooklyn operations. The total charge against earnings of approximately $3,220,000 resulting from eliminating the Brooklyn operation includes the lease termination payment of $1,150,000, a provision of $200,000 for plant repairs, the write-off of leasehold improvements of $1,778,000, severance and other costs for terminated employees of $730,000, less deferred rent previously expensed of $638,000.

INTEREST EXPENSE

Interest expense for 1999 increased by 121.9% over that of 1998 reflecting the issuance of an additional $17,800,000 of convertible debentures in 1999.

Interest expense for 1998 increased by 13% over that of 1997 reflecting the substantial new debt in the form of $25,800,000 of convertible debentures that was added in 1998.

AMORTIZATION OF DEFERRED DEBT DISCOUNT AND DEBT ISSUANCE COSTS

In 1999 and 1998 the Company issued warrants and incurred costs associated with private placements and bridge financings. The value of warrants issued in 1999 and 1998, as determined by use of the Black-Scholes valuation model, was $5,234,000 and $2,618,000, respectively. Additionally, the Company incurred approximately $907,000 and $1,516,000 of debt issuance costs in 1999 and 1998, respectively. These amounts are being amortized over the life of the underlying debentures which expire in March, 2003. Accordingly, the Company amortized $1,825,000 and $661,000 in 1999 and 1998, respectively.

OTHER INCOME

Included in other income for 1998 is $1,900,000 realized from the sale of certain assets to Mallinckrodt. This transaction was entered into in 1997 but the conditions for realization of the gain from the sale were not met until 1998.

LIQUIDITY AND CAPITAL RESOURCES

At December 31, 1999, the Company had cash and cash equivalents of $786,000 as compared to $1,850,000 at December 31, 1998. The Company had a working capital deficit at December 31, 1999 of $(5,181,000).

On May 26, 1999, the Company consummated a private offering of securities for an aggregate purchase price of up to $22.8 million (the "Oracle Offering"). The securities issued in the Oracle Offering consisted of 5% convertible senior secured debentures (the "1999 Debentures") and common stock purchase warrants (the "1999 Warrants"), each of which are substantially similar to the debentures and warrants issued by the Company in the Galen Offering completed in March, 1998. Of the $22.8 million to be invested pursuant to the Oracle Offering, $5 million was funded by Oracle Strategic Partners, L.P. ("Oracle") on May 26, 1999, the closing date of the Oracle Offering, with an additional $10 million to be funded by Oracle in two (2) installments of $5 million each. The first installment of the additional $10 million Oracle investment was funded on July 27, 1999. Pursuant to an agreement reached between the Company and Oracle on March 20, 2000, the final $5 million investment to be made by Oracle has been waived.

In addition to the $10 million investment made by Oracle, approximately $7,037,000 of the 1999 Debentures issued pursuant to the Oracle Offering were issued in exchange for the surrender of a like amount of principal and accrued interest outstanding under the Company's convertible promissory notes issues pursuant to various bridge loan transactions with Galen Partners III, L.P., Galen Partners International III, L.P., Galen Employee Fund III, L.P. (collectively, "Galen") and certain other investors in the aggregate amount of $10,104,110 during the period from August 1998 through and including May, 1999 (the "1999 Galen Bridge Loans"). The remaining balance of the 1999 Galen Bridge Loans in the principal amount of $3,495,000 plus accrued and unpaid interest was satisfied with a portion of the proceeds of the second $5 million installment of Oracle's investment funded on July 27, 1999. After giving effect to the satisfaction of approximately $7 million of indebtedness under the 1999 Galen Bridge Loans through the issuance of a like principal amount of 1999 Debentures, the repayment of the balance of the 1999 Galen Bridge Loans in the principal amount of approximately $3.5 million plus accrued and unpaid interest, and the waiver by the Company of the final $5 million installment to be made by Oracle pursuant to the Oracle Offering, the Company received net cash proceeds from the Oracle Offering of approximately $7.3 million.

The net proceeds from the issuance of the 1999 Debentures and 1999 Warrants pursuant to the Oracle Offering, in addition to satisfying the principal and accrued interest under the 1999 Galen Bridge Loans, were used to fund working capital, including the purchase of raw materials, payroll expenses and other Company operating expenses.

During the period from May 1997 through July 1997, the Company borrowed approximately $3 million from Mylan Laboratories, Inc. pursuant to five unsecured, demand promissory notes. The advances made by Mylan Laboratories, Inc. were part of a proposed investment by Mylan Laboratories, Inc. in the Company, including the proposed purchase of the Company's Houba Indiana facility as well as a partial tender offer for the Company's common stock. The Company used the proceeds of these borrowings for working capital. To date, $621,000 has been paid by the Company to Mylan against such indebtedness in the form of product deliveries to Mylan. Pursuant to an agreement reached between the parties, the Company is required to satisfy interest on the outstanding indebtedness on an annual basis while the indebtedness remains outstanding and to satisfy the principal amount of such indebtedness in the form of product deliveries to Mylan until such time as the indebtedness is satisfied in full.

In addition to the 1999 Galen Bridge Loans, the Company secured bridge financing from Galen in the aggregate amount of approximately $3,300,000, funded through six separate bridge loan transactions during the period from December 8, 1999 through March 29, 2000 (collectively, the "2000 Galen Bridge Loans"). The principal amount of the 2000 Galen Bridge Loans and accrued and unpaid interest were satisfied in full with a portion of the proceeds of the Watson Term Loan (as described below). Prior to repayment, the 2000 Galen Bridge Loans accrued interest at the rate of 18% per annum and were secured by a first lien on all of the Company's assets. In consideration for the extension of the 2000 Galen Bridge Loans, the Company issued common stock purchase warrants to Galen to purchase an aggregate of 150,000 shares of the Company's common stock (representing warrants to purchase 50,000 shares of common stock for each $1,000,000 in

principal amount of the 2000 Galen Bridge Loans). The warrants issued pursuant to the 2000 Galen Bridge Loans have an exercise price equal to the fair market value of the Company's common stock on the date of issuance and are substantially identical to those issued by the Company in the Oracle Offering. The 2000 Galen Bridge Loans were obtained by the Company in order to provide necessary working capital prior to the completion of the Watson Term Loan as described below.

On March 22, 2000, the Company executed a Lease Termination and Settlement Agreement with the landlord of the Company's Brooklyn, New York manufacturing facility (the "Settlement Agreement"). The Settlement Agreement accelerates the termination of the lease covering the Company's Brooklyn facility and provides the Company with the time necessary to transfer operations to the Company's Congers, New York facility and cease all manufacturing, research and development and warehouse operations currently conducted in Brooklyn. The Settlement Agreement provided for the termination of the Brooklyn lease on August 31, 2000, subject to the Company's right to extend the lease term to March 31, 2001. The original lease provided for a term expiring December 31, 2005 with a rental payment obligation of $6,715,000 during the period from September 1, 2000 through December 31, 2005. The Settlement Agreement provided for the Company's payment of a lease termination fee of $1,150,000, the advance payment of rent through August 31, 2000 and a restoration escrow deposit of $200,000 for plant repairs. The Company also deposited in escrow with its counsel $390,600 which represents rental payments for the period September 1, 2000 through March 31, 2001. Such escrow amount will be returned to the Company in the event it vacates the Brooklyn facility on or prior to August 31, 2000. The Company funded the termination fee payment, the advance rental payment obligations and restoration amount required pursuant to the Settlement Agreement with the proceeds received from the Watson Term Loan described below.

In addition to the lease termination and escrow payments described above, the Company estimates that it will incur severance and other costs for terminated employees of approximately $730,000 which are expected to be paid in the third quarter of 2000. Also, the Company expects to incur capital costs of approximately $500,000 associated with the transfer of certain operations from Brooklyn to the Congers facility.

In addition to the other strategic alliance transactions with Watson Pharmaceuticals, Inc. ("Watson") completed on March 29, 2000 (see "Item 1. Business - Recent Events - Strategic Alliance with Watson Pharmaceuticals"), the Company and Watson executed a Loan Agreement providing for Watson's extension of a $17,500,000 term loan to the Company (the "Watson Term Loan"). The Watson Term 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 advance. As of March 31, 2000, $9 million had been advanced by Watson to the Company under the Watson Term Loan. The Watson Term Loan is secured by a first lien on all of the Company's assets, senior to the liens securing all other Company indebtedness, carries a floating rate of interest equal to prime plus two percent and matures on March 31, 2003. At March 31, 2000, a portion of the net proceeds of the Watson Term Loan were used to satisfy in full the 2000 Galen Bridge Loans, to satisfy the Company's payment obligations under the Settlement Agreement with the landlord of its Brooklyn, New York facility and for working capital. The remaining net proceeds of the Watson 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 fund the relocation of the Company's research and development and manufacturing operations from its Brooklyn, New York facility to its Congers, New York facility and for working capital to fund continued operations.

The net proceeds from the Watson Term Loan has permitted the Company to satisfy its current liabilities and accounts payable. In addition, the net proceeds from the Watson Term Loan combined with the payments to be received by the Company from Watson under each of the Product Acquisition Agreement and the Core Products Supply Agreement will provide the Company with sufficient working capital to fund operations for at least the next twelve months.

CAPITAL EXPENDITURES

The Company's capital expenditures during 1999, 1998 and 1997 were $849,000 $1,545,000, and $85,000, respectively. The decrease in capital expenditures in 1999 as compared to prior years is attributable to the completion of certain equipment and facility upgrades that had been delayed in prior years due to the Company's cash conservation measures in those years. The Company has budgeted for capital expenditures approximately $2,500,000 in fiscal 2000. Such amounts will be funded from the net proceeds of the Watson Term Loan and the payments to be received by the Company pursuant to each of the Product Acquisition Agreement and Core Products Supply Agreement with Watson.

YEAR 2000 COMPLIANCE

In anticipation of the Year 2000, the Company installed a new information system, including hardware and software. To date, neither the Company nor any of its customers or suppliers has experienced any material Year 2000 failures relating to their computer systems.

IMPACT OF INFLATION

The Company believes that inflation did not have a material impact on its operations for the periods reported. Significant increases in labor, employee benefits and other expenses could have a material adverse effect on the Company's performance.

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA.

The response to this item is submitted as a separate section of this Report commencing on page F-1.

ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE.

Not Applicable.

PART III

ITEM 10. DIRECTORS AND EXECUTIVE OFFICERS OF THE REGISTRANT.

The information required by Item 10 will be included in the Company's Proxy Statement for the 2000 Annual Meeting of Shareholders, which will be filed within 120 days after the close of the Company's fiscal year ended December 31, 1999, and is hereby incorporated herein by reference to such Proxy Statement.

ITEM 11. EXECUTIVE COMPENSATION.

The information required by Item 11 will be included in the Company's Proxy Statement for the 2000 Annual Meeting of Shareholders, which will be filed within 120 days after the close of the Company's fiscal year ended December 31, 1999, and is hereby incorporated herein by reference to such Proxy Statement.

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT.

The information required by Item 12 will be included in the Company's Proxy Statement for the 2000 Annual Meeting of Shareholders, which will be filed within 120 days after the close of the Company's fiscal year ended December 31, 1999, and is hereby incorporated herein by reference to such Proxy Statement.

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS.

The information required by Item 13 will be included in the Company's Proxy Statement for the 2000 Annual Meeting of Shareholders, which will be filed within 120 days after the close of the Company's fiscal year ended December

31, 1999, and is hereby incorporated herein by reference to such Proxy Statement.

PART IV

ITEM 14. EXHIBITS, FINANCIAL STATEMENT SCHEDULES AND REPORTS ON FORM 8-K.

(a) Financial Statements--See Index to Financial Statements.

(b) Reports on Form 8-K

No reports on Form 8-K were filed during the last quarter of the fiscal year covered by this Annual Report on Form 10-K.

(c) Exhibits

The following exhibits are included as a part of this Annual Report on Form 10-K or incorporated herein by reference.

EXHIBIT NUMBER	DOCUMENT
*3.1	Certificate of Incorporation and amendments.
3.2	Restated Bylaws (incorporated by reference to Exhibit 3.1 to the Registrant's Quarterly Report on Form 10-Q for the quarter ended June 30, 1993).
3.3	Restated By-Laws (incorporated by reference to Exhibit 3.3 to the Registrant's Annual Report Form 10-K for the year ended December 31, 1998 (the "1998 Form 10-K")).
10.1	Credit Agreement, dated as of December 22, 1992, among the Registrant and The Chase Manhattan Bank, N.A. (incorporated by reference to Exhibit 10.1 to the Registrant's Annual Report on Form 10-K for the year ended December 31, 1992 (the "1992 Form 10-K")).
10.2	Amendment Two, dated as of January 12, 1994, to Credit Agreement among the Registrant and The Chase Manhattan Bank, N.A., together with forms of Stock Warrant and Registration Rights Agreement (incorporated by reference to Exhibit 10.1. to the Registrant's Annual Report on Form 10-K for the year ended December 31, 1993 (the "1993 Form 10-K")).
10.3	Amendment Three, dated as of May 31, 1994, to Credit Agreement among the Registrant and The Chase Manhattan Bank, N.A. (incorporated by reference to Exhibit 6(a) to the Registrant's Quarterly Report on Form 10-Q for the quarter ended March 31, 1994).
10.4	Amendment Four, dated as of July 1994, to Credit Agreement among the Registrant and The Chase Manhattan Bank, N.A. (incorporated by reference to Exhibit 6(a) to the Registrant's Quarterly Report on Form 10-Q for the quarter ended June 30, 1994).
10.5	Amendment Five, dated as of March 21, 1995, to Credit Agreement among the Registrant and The Chase Manhattan Bank, N.A. (incorporated by reference to Exhibit 10.7 to the Registrant's Current Report on Form 8-K dated March 21, 1995 (the "March 8-K")).

EXHIBIT NUMBER	DOCUMENT
10.5(l)	Form of Warrants issued to The Bank of New York, The Chase Manhattan Bank, N.A. and the Israel Discount Bank (incorporated by reference to Exhibit 10.5(i) to the Registrant's Annual Report on Form 10-K for the year ended December 31, 1995 (the "1995 Form 10-K")).
10.5(2)	Letter Agreement, dated July 10, 1995, among Halsey Drug Co., Inc., The Chase Manhattan Bank, N.A., The Bank of New York and Israel Discount Bank of New York (incorporated by reference to Exhibit 6(a) to the Registrant's Quarterly Report on Form 10-Q for the quarter ended June 30, 1995 (the "June 10-Q")).
10.5(3)	Letter Agreement, dated November 16, 1995, among Halsey Drug Co., Inc., The Chase Manhattan Bank, N.A., The Bank of New York and Israel Discount Bank of New York (incorporated by reference to Exhibit 10.25(iv) to the 1995 10-K).
10.5(4)	Amendment 6, dated as of August 6, 1996, to Credit Agreement among Halsey Drug Co., Inc., The Chase Manhattan Bank, N.A., The Bank of New York and Israel Discount Bank of New York (incorporated by reference to Exhibit 10.1 to Amendment No. 1 to the Registrant's Quarterly Report on Form 10-Q for the quarter ended June 30, 1996 (the "June 1996 10-Q").
10.5(5)	Letter Agreement, dated March 25, 1997 among Halsey Drug Co., Inc., The Chase Manhattan Bank, as successor in interest to The Chase Manhattan Bank (National Association), The Bank of New York and Israel Discount Bank.
10.6	Agreement Regarding Release of Security Interests dated as of March 21, 1995 by and among the Company, Mallinckrodt Chemical Acquisition, Inc. and The Chase Manhattan Bank, N.A. (incorporated by reference to Exhibit 10.9 of the March 8-K).
10.7	Consulting Agreement dated as of September, 1993 between the Registrant and Joseph F. Limongelli (incorporated by reference to Exhibit 10.6 to the 1993 Form 10-K).
10.8	Employment Agreement, dated as of January 1, 1993, between the Registrant and Rosendo Ferran (incorporated by reference to Exhibit 10.2 to the 1992 Form 10-K).
10.10(1)	Halsey Drug Co., Inc. 1984 Stock Option Plan, as amended (incorporated by reference to Exhibit 10.3 to the 1992 Form 10-K).
10.10(2)	Halsey Drug Co., Inc. 1995 Stock Option and Restricted Stock Purchase Plan (incorporated by reference to Exhibit 4.1 to the Registrant's Registration Statement on Form S-8, File No. 33-98396).
10.10(3)	Halsey Drug Co., Inc. Non-Employee Director Stock Option Plan.
10.11	Leases, effective February 13, 1989 and January 1, 1990, respectively, among the Registrant and Milton J. Ackerman, Sue Ackerman, Lee Hinderstein, Thelma Hinderstein and Marilyn Weiss (incorporated by reference to Exhibits 10.6 and 10.7, respectively, to the Registrant's Annual Report on Form 10-K for the year ended December 31, 1989).
10.12	Lease, effective as of April 15, 1988, among the Registrant and Milton J. Ackerman, Sue Ackerman, Lee Hinderstein, Thelma Hinderstein and Marilyn Weiss, and Rider thereto (incorporated by reference to Exhibit 10.12 to the Registrant's Annual Report on Form 10-K for the year ended December 31, 1987).

EXHIBIT NUMBER	DOCUMENT
10.12(l)	Lease, as of October 31, 1994, among Registrant and Milton J. Ackerman, Sue Ackerman, Lee Hinderstein, Thelma Hinderstein and Marilyn Weiss, together with Modification, Consolidation and Extension Agreement (incorporated by reference to Exhibit 10. 12(i) to the 1995 Form 10-K).
10.13	Asset Purchase Agreement dated as of March 21, 1995 among Mallinckrodt Chemical Acquisition, Inc. ("Acquisition"), Mallinckrodt Chemical, Inc., as guarantor and the Registrant (incorporated by reference to Exhibit 10.1 to the March 8-K).
10.14	Toll Manufacturing Agreement for APAP/Oxycodone Tablets dated as of March 21, 1995 between Acquisition and the Registrant (incorporated by reference to Exhibit 10.2 to the March 8-K).
10.15	Capsule ANDA Option Agreement dated as of March 21, 1995 between Acquisition and the Registrant (incorporated by reference to Exhibit 10.3 to the March 8-K).
10.16	Tablet ANDA Noncompetition Agreement dated as of March 21, 1995 between the Registrant and Acquisition (incorporated by reference to Exhibit 10.4 to the March 8-K).
10.17	Subordinated Non-Negotiable Promissory Term Note in the amount of $1,200,00 dated March 21, 1995 issued by the Registrant to Acquisition (incorporated by reference to Exhibit 10.5 to the March 8-K).
10.18	Term Note Security Agreement dated as of March 21, 1995 among the Company, Houba, Inc. and Acquisition (incorporated by reference to Exhibit 10.6 to the March 8-K).
10.19	Amendment dated March 21, 1995 to Subordination Agreement dated as of July 21, 1994 between Mallinckrodt Chemical, Inc., Mallinckrodt Chemical Acquisition, Inc., the Registrant, The Chase Manhattan Bank (National Association), Israel Discount Bank of New York, The Bank of New York, and The Chase Manhattan Bank (National Association) (incorporated by reference to Exhibit 10.8 to the March 8-K).
10.20	Agreement dated as of March 30, 1995 between the Registrant and Zatpack, Inc. (incorporated by reference to Exhibit 10.10 to the March 8-K).
10.21	Waiver and Termination Agreement dated as of March 30, 1995 between Zuellig Group, W.A., Inc. and Indiana Fine Chemicals Corporation (incorporated by reference to Exhibit 10.11 to the March 8-K).
10.22	Convertible Subordinated Note of the Registrant dated December 1, 1994 issued to Zatpack, Inc. (incorporated by reference to Exhibit 10.12 to the March 8-K).
10.23	Agreement dated as of March 30, 1995 among the Registrant, Indiana Fine Chemicals Corporation, Zuellig Group, N.A., Inc., Houba Inc., Zetapharm, Inc. and Zuellig Botanical, Inc. (incorporated by reference to Exhibit 10.13 to the March 8-K).
10.24	Supply Agreement dated as of March 30, 1995 between Houba, Inc. and ZetaPharm, Inc. (incorporated by reference to Exhibit 10.14 to the March 8-K).
10.25	Form of 10% Convertible Subordinated Debenture (incorporated by reference to Exhibit 6(a) to the June 10-Q).

EXHIBIT NUMBER	DOCUMENT
10.26	Form of Redeemable Common Stock Purchase Warrant (incorporated by reference to Exhibit 6(a) to the June 10-Q).
10.27	Form of 10% Convertible Subordinated Debenture (incorporated by reference to Exhibit 4.1 to the Registrant's Current Report on Form 8-K dated December 4, 1995 (the "December 8-K")).
10.28	Form of Redeemable Common Stock Purchase Warrant (incorporated by reference to Exhibit 4.2 to the December 8-K).
10.29	Form of 10% Convertible Subordinated Debenture (incorporated by reference to Exhibit 99 to the June 1996 10-Q).
10.30	Form of Redeemable Common Stock Purchase Warrant (incorporated by reference to Exhibit 4.1 to Amendment No. 1 to the June 1996 10-Q).
10.31	Form of 5% Convertible Senior Secured Debenture (incorporated by reference to Exhibit 4.1 to the Registrant's Current Report on Form 8-K dated March 24, 1998 (the "March 1998 8-K")).
10.32	Form of Common Stock Purchase Warrant (incorporated by reference to Exhibit 4.2 to the March 1998 8-K).
10.33	Debenture and Warrant Purchase Agreement dated March 10, 1998, by and among the Registrant, Galen Partners III, L.P. and the other Purchasers listed on the Signature Page thereto (incorporated by reference to Exhibit 10.1 to the March 1998 8-K).
10.34	Form of General Security Agreement of Halsey Drug Co., Inc. dated March 10, 1998 (incorporated by reference to Exhibit 10.2 to the March 1998 8-K).
10.35	Form of Agreement of Guaranty of Subsidiaries of Halsey Drug Co., Inc. dated March 10, 1998 (incorporated by reference to Exhibit 10.3 to the March 1998 8-K).
10.36	Form of Guarantor General Security Agreement dated March 10, 1998 (incorporated by reference to Exhibit 10.4 to the March 1998 8-K).
10.37	Stock Pledge Agreement dated March 10, 1998 by and between the Registrant and Galen Partners III, L.P., as agent (incorporated by reference to Exhibit 10.5 to the March 1998 8-K).
10.38	Form of Irrevocable Proxy Agreement (incorporated by reference to Exhibit 10.6 to the March 1998 8-K).
10.39	Agency Letter Agreement dated March 10, 1998 by and among the Purchasers a party to the Debenture and Warrant Purchase Agreement, dated March 10, 1998 (incorporated by reference to Exhibit 10.7 to the March 1998 8-K).
10.40	Press Release of Registrant dated March 13, 1998 (incorporated by reference to Exhibit 99.1 to the March 1998 8-K).
10.41	Current Report on Form 8-K as filed by the Registrant with the Securities and Exchange Commission on March 24, 1998.

EXHIBIT NUMBER	DOCUMENT
10.42	Letter Agreement between the Registrant and the U.S. Department of Justice dated March 27, 1998 relating to the restructuring of the fine assessed by the Department of Justice under the Plea Agreement dated June 21, 1993.
10.43	Employment Agreement dated as of March 10, 1998 between the Registrant and Michael K. Reicher (incorporated by reference to Exhibit 10.43 to the Registrant's Annual Report of Form 10-K for the year ended December 31, 1997 (the "1997 Form 10-K")).
10.44	Employment Agreement dated as of March 10, 1998 between the Registrant and Peter Clemens (incorporated by reference to Exhibit 10.44 to the 1997 Form 10-K.
10.45	Amended, Restated and Consolidated Bridge Loan Agreement dated as of December 2, 1998 between the Company, Galen Partners III, L.P., Galen Partners International III, L.P., Galen Employee Fund III, L.P. and the other signatures thereto (incorporated by reference to Exhibit 10.45 to the 1998 Form 10-K).
10.46	First Amendment to Amended, Restated and Consolidated Bridge Loan Agreement dated December 7, 1998 between the Company and the lenders listed on the signature page thereto (incorporated by reference to Exhibit 10.46 to the 1998 Form 10-K).
10.47	Second Amendment to Amended, Restated and Consolidated Bridge Loan Agreement dated March 8, 1999 between the Company and the lenders listed on the signature page thereto (incorporated by reference to Exhibit 10.47 to the 1998 Form 10-K).
10.48	Form of 10% Convertible Secured Note due May 30, 1999 (incorporated by reference to Exhibit 10.48 to the 1998 Form 10-K).
10.49	Form of Common Stock Purchase Warrant issued pursuant to be Amended, Restated and Consolidated Bridge Loan Agreement (incorporated by reference to Exhibit 10.49 to the 1998 Form 10-K).
10.50	Amended and Restated General Security Agreement dated December 2, 1998 between the Company and Galen Partners III, L.P., as Agent (incorporated by reference to Exhibit 10.50 to the 1998 Form 10-K).
10.51	Subordination Agreement dated December 2, 1998 between the Registrant and Galen Partners III, L.P., as Agent (incorporated by reference to Exhibit 10.51 to the 1998 Form 10-K).
10.52	Agency Letter Agreement dated December 2, 1998 by and among the lenders a party to the Amended, Restated and Consolidated Bridge Loan Agreement, as amended (incorporated by reference to Exhibit 10.52 to the 1998 Form 10-K).
10.53	Lease Agreement dated March 17, 1999 between the Registrant and Par Pharmaceuticals, Inc. (incorporated by reference to Exhibit 10.53 to the 1998 Form 10-K).
10.54	Lease Agreement dated September 1, 1998 between the Registrant and Crimson Ridge Partners (incorporated by reference to Exhibit 10.54 to the 1998 Form 10-K).
10.55	Manufacturing and Supply Agreement dated March 17, 1999 between the Registrant and Par Pharmaceuticals, Inc. (incorporated by reference to Exhibit 10.55 to the 1998 Form 10-K).

EXHIBIT NUMBER	DOCUMENT
10.56	Halsey Drug Co., Inc. 1998 Stock Option Plan (incorporated by] reference to Exhibit 10.56 to the 1998 Form 10-K).
10.57	Loan Agreement dated March 29, 2000 between the Registrant and Watson Pharmaceuticals, Inc. (incorporated by reference to Exhibit 10.57 to the Registrant's Current Report on Form 8-K dated March 29, 2000 (the "March 2000 8-K")). +
10.58	Amendment to Loan Agreement dated March 31, 2000 between the Registrant and Watson Pharmaceuticals, Inc. (incorporated by reference to Exhibit 10.58 to the March 2000 8-K).
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. (incorporated by reference to Exhibit 10.59 to the March 2000 8-K).
10.60	Watson Security Agreement dated March 29, 2000 between the Registrant and Watson Pharmaceuticals, Inc. (incorporated by reference to Exhibit 10.60 to the March 2000 8-K).
10.61	Stock Pledge Agreement dated March 29, 2000 between the Registrant and Watson Pharmaceuticals, Inc. (incorporated by reference to Exhibit 10.61 to the March 2000 8-K).
10.62	Watson Guarantee dated March 29, 2000 between Houba, Inc. and Watson Pharmaceuticals, Inc., as the guarantors, in favor of Watson Pharmaceuticals, Inc. (incorporated by reference to Exhibit 10.62 to the March 2000 8-K).
10.63	Watson's Guarantors Security Agreement dated March 29, 2000 between Halsey Pharmaceuticals, Inc., Houba, Inc. and Watson Pharmaceuticals, Inc. (incorporated by reference to Exhibit 10.63 to the March 2000 8-K).
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. (incorporated by reference to Exhibit 10.64 to the March 2000 8-K).+
10.65	Real Estate Mortgage dated March 29, 2000 between Houba, Inc. and Watson Pharmaceuticals, Inc. (incorporated by reference to Exhibit 10.65 to the March 2000 8-K).
10.66	Subordination Agreement by and among Houba, Inc., Galen Partners, III, L.P., Oracle Strategic Partners, L.P. and Watson Pharmaceuticals, Inc. (incorporated by reference to Exhibit 10.66 to the March 2000 8-K).
10.67	Product Purchase Agreement dated March 29, 2000 between the Registrant and Watson Pharmaceuticals, Inc. (incorporated by reference to Exhibit 10.67 to the March, 2000 8-K). +
10.68	Finished Goods Supply Agreement dated March 29, 2000 between the Registrant and Watson Pharmaceuticals, Inc. (incorporated by reference to Exhibit 10.68 to the March 2000 8-K). +
10.69	Active Ingredient Supply Agreement dated March 29, 2000 between the Registrant and Watson Pharmaceuticals, Inc. (incorporated by reference to Exhibit 10.69 to the March 2000 8-K). +

EXHIBIT NUMBER	DOCUMENT
10.70	Right of First Negotiation Agreement dated March 29, 2000 between the Registrant and Watson Pharmaceuticals, Inc. (incorporated by reference to Exhibit 10.70 to the March 2000 8-K). +
10.71	Finished Goods Supply Agreement (Core Products) dated March 29, 2000 between the Registrant and Watson Pharmaceuticals, Inc. (incorporated by reference to Exhibit 10.71 to the March 2000 8-K). +
*10.72	Debenture and Warrant Purchase Agreement dated May 26, 1999 by and among the Registrant, Oracle Strategic Partners, L.P. and the other purchasers listed on the signature page thereto (the "Oracle Purchase Agreement").
*10.73	Form of 5% Convertible Senior Secured Debenture issued pursuant to the Oracle Purchase Agreement.
*10.74	Form of Common Stock Purchase Warrant issued pursuant to the Oracle Purchase Agreement.
*10.75	Lease Termination and Settlement Agreement dated March 20, 2000 between the Registrant and Atlantic Properties Company in respect of the Registrant's Brooklyn, New York leased facility.
21	Subsidiaries of the Registrant (incorporated by reference to Exhibit 22 to the 1993 Form 10-K).
*23.1	Consent of Grant Thornton LLP, independent certified public accountants.
*27	Financial Data Schedule, which is submitted electronically to the Securities and Exchange Commission for informational purposes only and not filed.

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

SIGNATURES

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

HALSEY DRUG CO., INC.

By: /s/ MICHAEL REICHER

Michael Reicher, President and Chief Executive Officer (Principal Executive Officer)

Date: April 14, 2000

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

/s/ WILLIAM G. SKELLY William G. Skelly	Chairman and Director	April 14, 2000
/s/ MICHAEL REICHER Michael Reicher	President, Chief Executive Officer and Director (Principal Executive Officer)	April 14, 2000
/s/ PETER CLEMENS Peter Clemens	Vice President, Chief Financial Officer (Principal Financial and accounting Officer) and Director	April 14, 2000
/s/ ALAN J. SMITH Alan J. Smith	Director	April 14, 2000
/s/ BRUCE F. WESSON Bruce F. Wesson	Director	April 14, 2000
/s/ WILLIAM SUMNER William Sumner	Director	April 14, 2000
/s/ SRINI CONJEEVARAM Srini Conjeevaram	Director	April 14, 2000
/s/ ZUBEEN SHROFF Zubeen Shroff	Director	April 14, 2000
/s/ Joel Liffman Joel Liffman	Director	April 14, 2000

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INDEX TO FINANCIAL STATEMENTS

REPORT OF INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS

Board of Directors
HALSEY DRUG CO., INC.

We have audited the accompanying consolidated balance sheets of Halsey Drug Co., Inc. and Subsidiaries as of December 31, 1999 and 1998, and the related consolidated statements of operations, stockholders' equity and cash flows for each of the three years in the period ended December 31, 1999. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Halsey Drug Co., Inc. and Subsidiaries as of December 31, 1999 and 1998, and the consolidated results of their operations and their consolidated cash flows for each of the three years in the period ended December 31, 1999, in conformity with accounting principles generally accepted in the United States.

GRANT THORNTON LLP

New York, New York
March 30, 2000

Halsey Drug Co., Inc. and Subsidiaries

CONSOLIDATED BALANCE SHEETS

December 31,
(in thousands)

	1999	1998
CURRENT ASSETS		
Cash	$ 786	$ 1,850
Accounts receivable - trade, net of allowances for doubtful accounts of $425 and $280 in 1999 and 1998, respectively	2,716	1,439
Inventories	3,502	6,354
Prepaid expenses and other current assets	213	148
Total current assets	7,217	9,791
PROPERTY, PLANT AND EQUIPMENT, NET	3,013	4,787
DEFERRED PRIVATE OFFERING COSTS	1,623	1,700
OTHER ASSETS AND DEPOSITS	642	135
	$12,495	$16,413

The accompanying notes are an integral part of these statements.

Halsey Drug Co., Inc. and Subsidiaries

CONSOLIDATED BALANCE SHEETS (CONTINUED)

December 31,
(in thousands)

	1999	1998
CURRENT LIABILITIES		
Notes payable	$ 4,038	$ 10,850
Accounts payable	2,283	1,834
Accrued expenses	5,777	3,972
Department of Justice Settlement	300	300
Total current liabilities	12,398	16,956
CONVERTIBLE SUBORDINATED DEBENTURES, NET	41,096	26,186
OTHER LIABILITIES		549
DEPARTMENT OF JUSTICE SETTLEMENT	1,375	1,675
COMMITMENTS AND CONTINGENCIES		
STOCKHOLDERS' EQUITY (DEFICIT)		
Common stock - $.01 par value; authorized, 80,000,000 shares; issued 14,829,511 shares and 14,443,212 shares in 1999 and 1998, respectively	148	144
Additional paid-in capital	35,751	29,113
Accumulated deficit	(77,284)	(57,221)
	(41,385)	(27,964)
Less treasury stock - at cost (439,603 shares)	(989)	(989)
	(42,374)	(28,953)
	$ 12,495	$ 16,413

The accompanying notes are an integral part of these statements.

Halsey Drug Co., Inc. and Subsidiaries

CONSOLIDATED STATEMENTS OF OPERATIONS

Year ended December 31,
(in thousands, except per share data)

	1999	1998	1997
Net sales	$ 11,420	$ 8,841	$ 9,088
Cost of goods sold	15,316	12,712	15,406
Gross margin	(3,896)	(3,871)	(6,318)
Operating costs			
Research and development	1,075	651	979
Selling, general and administrative expenses	7,383	8,078	6,308
Plant shutdown costs	3,220		
Total operating costs	(11,678)	(8,729)	(7,287)
Loss from operations	(15,574)	(12,600)	(13,605)
Other income(expense)			
Interest expense	(2,851)	(1,285)	(1,017)
Amortization of deferred debt discount and private offering costs	(1,825)	(661)	(127)
Other	187	1,822	(264)
	(4,489)	(124)	(1,408)
NET LOSS	$(20,063)	$(12,724)	$(15,013)
Basic and diluted loss per common share	$ (1.40)	$ (.92)	$ (1.12)
Weighted average number of outstanding shares	14,326	13,813	13,434

The accompanying notes are an integral part of these statements.

Halsey Drug Co., Inc. and Subsidiaries

CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY

Years ended December 31, 1999, 1998 and 1997
(in thousands)

	Common stock, $.01 par value		Additional paid-in	Accumulated	Treasury stock, at cost		
	Shares	Amount	capital	deficit	Shares	Amount	Total
Balance at December 31, 1996	13,176	$ 131	$ 23,316	$(29,484)	(475)	$ (1,044)	$ (7,081)
Issuance of common stock - conversion of debentures	643	7	1,529				1,536
Issuance of shares as payment of Interest	69	1	224				225
Sale of treasury stock	25		45		35	55	100
Exercise of warrants of convertible debentures	22		72				72
Stock options exercised	95	1	303				304
Net loss for the year ended December 31, 1997				(15,013)			(15,013)
Balance at December 31, 1997 (carried forward)	14,030	140	25,489	(44,497)	(440)	(989)	(19,857)

Halsey Drug Co., Inc. and Subsidiaries

CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY (CONTINUED)

Years ended December 31, 1999, 1998 and 1997
(in thousands)

	Common stock, $.01 par value		Additional paid-in	Accumulated	Treasury stock, at cost		
	Shares	Amount	capital	deficit	Shares	Amount	Total
Balance at December 31, 1997 (brought forward)	14,030	$ 140	$ 25,489	$(44,497)	(440)	$ (989)	$(19,857)
Issuance of common stock - conversion of notes payable	110	1	213				214
Issuance of shares as payment of interest	263	3	592				595
Issuance of common stock - settlement of trade payables	40		55				55
Deferred debt discount on warrants issued with convertible debentures			2,764				2,764
Net loss for the year ended December 31, 1998				(12,724)			(12,724)
Balance at December 31, 1998 (carried forward)	14,443	144	29,113	(57,221)	(440)	(989)	(28,953)

Halsey Drug Co., Inc. and Subsidiaries

CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY (CONTINUED)

Years ended December 31, 1999, 1998 and 1997
(in thousands)

	Common stock, $.01 par value		Additional paid-in	Accumulated	Treasury stock, at cost		
	Shares	Amount	capital	deficit	Shares	Amount	Total
Balance at December 31, 1998 (brought forward)	14,443	$ 144	$ 29,113	$(57,221)	(440)	$ (989)	$(28,953)
Issuance of shares as payment of interest	322	3	524				527
Deferred debt discount on warrants and private issuance costs			5,641				5,641
Warrants issued for acquisition of ANDA			350				350
Exercise of warrants	29	1	49				50
Issuance of common stock as payment of legal fees	26		50				50
Issuance of common stock as payment of payables	10		24				24
Net loss for the year ended December 31, 1999				(20,063)			(20,063)
BALANCE AT DECEMBER 31, 1999	14,830	$ 148	$ 35,751	$(77,284)	(440)	$ (989)	$(42,374)

The accompanying notes are an integral part of this statement.

Halsey Drug Co., Inc. and Subsidiaries

CONSOLIDATED STATEMENTS OF CASH FLOWS

Year ended December 31,
(in thousands)

	1999	1998	1997
Cash flows from operating activities			
Net loss	$(20,063)	$(12,724)	$(15,013)
Adjustments to reconcile net loss to net cash used in operating activities			
Depreciation and amortization	914	1,113	1,606
Amortization of deferred debt discount and private offering costs	1,825	661	127
Provision for losses on accounts receivable	145	(262)	118
Loss on disposal of assets	1,709	170	38
Stock issued for legal expense	50		
Stock issued for trade payables	24		
Debentures and stock issued for interest expense	939		
Changes in assets and liabilities			
Accounts receivable	(1,422)	(1,115)	45
Inventories	2,852	(3,898)	1,302
Prepaid expenses and other current assets	(65)	126	165
Other assets and deposits	(157)		
Accounts payable	399	(4,197)	1,851
Deferred gain		(1,900)	
Other liabilities	(549)		
Accrued expenses	1,444	(2,665)	4,553
Total adjustments	8,108	(11,967)	9,805
Net cash used in operating activities	(11,955)	(24,691)	(5,208)
Cash flows from investing activities			
Capital expenditures	(918)	(1,545)	(85)
Net proceeds from sale of assets	69	96	
Collection of notes receivable			1,000
Net cash provided by(used in) investing activities	(849)	(1,449)	915
Cash flows from financing activities			
Proceeds from issuance of notes payable	4,000	6,495	3,881
Reissuance of treasury stock			70
Payments to Department of Justice	(300)	(178)	
Bank overdraft		(159)	(127)
Due to banks		(2,476)	
Payments on notes payable, net	(9,464)		
Proceeds from issuance of convertible subordinated Debentures	17,862	25,800	
Proceeds from exercise of stock warrants	49		377
Deferred private offering costs	(407)	1,518	
Net cash provided by financing activities	11,740	27,964	4,201
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	(1,064)	1,824	(92)
Cash and cash equivalents at beginning of year	1,850	26	118
Cash and cash equivalents at end of year	$ 786	$ 1,850	$ 26

Halsey Drug Co., Inc. and Subsidiaries

CONSOLIDATED STATEMENTS OF CASH FLOWS (CONTINUED)

Year ended December 31,
(in thousands)

Supplemental disclosures of noncash activities:

Year ended December 31, 1999

1. The Company issued 321,777 shares of common stock as payment for $526,779 in accrued interest.

2. The Company issued 26,106 shares of common stock as payment for $50,500 in legal fees and 9,846 shares of common stock as payment for $24,000 in trade payables.

3. The Company issued approximately 3,608,604 warrants (Note G) valued and recorded in the aggregate as $5,234,000 of unamortized debt discount and a reduction in the amount of the related obligation.

4. The Company converted approximately $6,609,000 of notes payable and approximately $428,000 of accrued interest on notes payable into convertible subordinated debentures.

5. The Company converted approximately $939,000 of accrued interest due from convertible subordinated debentures into additional debentures.

6. The Company issued 1,022,284 warrants for funding fees valued and recorded as $907,000 in deferred private issuance costs.

7. The Company issued 500,000 warrants to Barr Laboratories, Inc.(to purchase of the rights to 50 pharmaceutical products) valued and recorded as $350,000 for the acquisition of certain product rights.

Year ended December 31, 1998

1. The Company issued 262,836 shares of common stock as payment for $593,313 in accrued interest.

2. The Company reissued 20,000 shares of common stock as payment for $25,000 in legal fees and 20,000 shares of common stock as payment for $30,000 in trade payables.

3. The Company issued 110,658 shares of common stock as payment of outstanding notes payable in amounts of $214,000 and $1,782 in accrued interest.

4. The Company issued approximately 5,500,086 warrants (Note G) valued and recorded in the aggregate as $2,263,434 of unamortized debt discount and a reduction in the amount of the related obligation.

Year ended December 31, 1997

1. The Company issued 25,000 shares of common stock as payment for $225,452 in accrued interest.

2. The Company issued 642,407 shares of common stock to Zatpack, Inc. as payment for an outstanding note payable in the amount of $1,536,000.

3. The Company reissued 25,000 shares of treasury stock as payment for $30,000 in consulting fees and the receipt of $70,000 in cash.

4. The Company recorded the satisfaction of $1,400,000 of subordinated promissory notes, related accrued interest of $200,000 and accounts payable of $300,000 due to a supplier, in lieu of the supplier paying $1,900,000 owed to the Company as described in Note K.

The accompanying notes are an integral part of these statements.

Halsey Drug Co., Inc. and Subsidiaries

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 1999, 1998 and 1997

NOTE A - SUMMARY OF ACCOUNTING POLICIES

Halsey Drug Co., Inc. (the "Company" or "Halsey"), a New York corporation established in 1935, and its subsidiaries are engaged in the manufacture, sale and distribution of generic drugs. The Company sells its generic drug products under its Halsey label and under private-label arrangements with drug store chains and drug wholesalers throughout the United States.

A summary of the significant accounting policies consistently applied in the preparation of the accompanying consolidated financial statements follows.

1. Principles of Consolidation and Basis of Presentation

The consolidated financial statements include 100% of the accounts of the Company and its wholly-owned subsidiaries, Blue Cross Products Co., Inc., Houba, Inc., Halsey Pharmaceuticals, Inc., Indiana Fine Chemicals Corporation, Cenci Powder Products, Inc., H.R. Cenci Laboratories, Inc., and The Medi-Gum Corporation. Except for Houba, Inc., all of the other subsidiaries are inactive. All material intercompany accounts and transactions have been eliminated.

2. Inventories

Inventories are stated at the lower of cost or market; cost is determined using the first-in, first-out method.

3. Property, Plant and Equipment

Property, plant and equipment are stated at cost less accumulated depreciation and amortization. Depreciation and amortization are provided for in amounts sufficient to relate the cost of depreciable assets to operations over their estimated service lives, principally on a straight-line basis. The estimated lives used in determining depreciation and amortization are:

Buildings	25 years
Machinery and equipment	5 - 10 years

Leasehold improvements were written off during the year. (See Note J).

NOTE A (CONTINUED)

4. Deferred Debt Discount and Private Issuance Costs

Debt discount resulting from the issuance of stock warrants in connection with the issuance of subordinated debt (Note G) is recorded as a reduction of the related obligations and is amortized over the remaining life of the related obligations. Debt discount is determined by a calculation which is based, in part, by the fair valued ascribed to such warrants determined by an independent valuation or management's use of the Black-Scholes valuation model. Deferred private issuance costs resulting from the issuance of warrants in connection with the extension of bridge loan maturity dates are recorded as deferred assets and amortized as additional interest expense over the remaining life of the related obligations.

5. Income Taxes

The Company accounts for income taxes utilizing an asset liability method for financial accounting and reporting for income taxes. Under this method, deferred tax assets and liabilities are determined based on differences between financial reporting and tax bases of assets and liabilities and are measured using the enacted tax rates and laws that will be in effect when the differences are expected to reverse.

6. Statements of Cash Flows

For purposes of the statements of cash flows, the Company considers all highly liquid debt instruments purchased with an original maturity of three months or less to be cash equivalents. The Company paid no substantial income taxes for the years ended December 31, 1999, 1998 and 1997. In addition, the Company paid interest of approximately $720,000, $1,946,000 and $1,113,000, respectively, for the years ended December 31, 1999, 1998 and 1997.

7. Use of Estimates in Consolidated Financial Statements

In preparing consolidated financial statements in conformity with generally accepted accounting principles, management makes estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements, as well as the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

NOTE A (CONTINUED)

8. Research and Development Costs

All research and development costs, including payments related to licensing agreements on products under development and research consulting agreements are expensed when incurred.

9. Impairment of Long-Lived Assets

The Company reviews long-lived assets and certain identifiable intangibles held and used for possible impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. See Note J for the impairment charge related to the write-off of leasehold improvements of the Company's Brooklyn New York Plant.

10. Stock-Based Compensation

The Company accounts for stock-based compensation under Statement of Financial Accounting Standards No. 123 ("SFAS No. 123"), "Accounting for Stock-Based Compensation," and continues to apply APB Opinion No. 25, "Accounting for Stock Issued to Employees," and related interpretations in accounting for its plans (Note M).

Equity instruments issued to nonemployees in exchange for goods and/or services are accounted for under the fair value method of SFAS No. 123.

11. Earnings (Loss) Per Share

The computation of basic earnings (loss) per share of common stock is based upon the weighted average number of common shares outstanding during the period. Diluted earnings per share is presented, and is equal to basic earnings per share for all years presented as the effect of other potentially dilutive securities would be antidilutive (Note M).

12. Revenue Recognition

Revenue is recognized from sales when title to product passes to customers.

13. Reclassifications

Certain reclassifications have been made to the 1998 and 1997 presentations to conform to the 1999 presentation.

NOTE B - LIQUIDITY MATTERS

At December 31, 1999, the Company had a working capital deficiency of approximately $5,181,000, had an accumulated deficit of approximately $77,284,000 and had incurred a loss of approximately $20,063,000 for the year then ended.

During 1999 the Company used the net proceeds from its 1999 private issuances of debentures and warrants (Note G) to satisfy the principal and accrued interest requirements of prior issued debentures and in addition, used such proceeds to fund working capital, including the purchase of raw materials, payroll expenses and other Company operating expenses.

On March 29, 2000, the Company completed various strategic alliance transactions with Watson Pharmaceuticals, Inc. ("Watson"). The transactions with Watson provided for (i) Watson's purchase, for $13,500,000, of a certain pending ANDA from the Company, (ii) Watson's rights to negotiate for Halsey to manufacture and supply certain identified future products to be developed by Halsey, (iii) Watson's marketing and sale of the Company's core products and (iv) Watson's extension of a $17,500,000 term loan to the Company.

The net proceeds from the Watson Term Loan has permitted the Company to satisfy its current liabilities and accounts payable. In addition, management believes the net proceeds from the Watson Term Loan combined with the payments to be received by the Company from Watson under each of the Product Acquisition Agreement and the Core Products Supply Agreement will provide the Company with sufficient working capital to fund operations for at least the next twelve months.

NOTE C - FAIR VALUE OF FINANCIAL INSTRUMENTS

Long-term and Short-term Debt and senior convertible subordinated debentures

The fair value of the Company's long-term and short-term debt and Senior Convertible Subordinated Debentures cannot be made without incurring excessive costs.

NOTE D - INVENTORIES

Inventories consist of the following:

	December 31,	
	1999	1998
	(in thousands)	
Finished goods	$ 725	$2,675
Work-in-process	720	1,166
Raw materials	2,057	2,513
	$3,502	$6,354

NOTE E - PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment are summarized as follows:

	December 31,	
	1999	1998
	(in thousands)	
Machinery and equipment	$12,893	$12,278
Leasehold improvements	325	6,103
Building	747	747
Land	44	44
	14,009	19,172
Less accumulated depreciation and amortization	10,996	14,385
	$ 3,013	$ 4,787

Depreciation and amortization expense for the years ended December 31, 1999, 1998 and 1997 was approximately $914,000, $1,113,000 and $1,606,000, respectively.

NOTE F- ACCRUED EXPENSES

Accrued expenses are summarized as follows:

	December 31,	
	1999	1998
	(in thousands)	
Payroll taxes payable	$1,503	$1,714
Rent	1,454	
Interest	764	619
Accrued payroll	736	92
Professional fees	362	539
Other	958	1,008
	$5,777	$3,972

At December 31, 1999, payroll taxes payable include approximately $1,467,000 and $31,000 of delinquent payroll taxes (including penalties and interest) due to the Internal Revenue Service and the State of New York, respectively, all of which liability was incurred in 1997 and 1996. The Company expects that the Federal liability will be partially offset by income tax refund claims which were filed and are pending before the IRS. Until such time as the IRS completes its review, the Company has not recorded any expected tax refund claims. The Company has negotiated a payment plan with the State of New York and the balance will be paid by the end of 2000.

NOTE G - CONVERTIBLE SUBORDINATED DEBENTURES AND STOCK WARRANTS

At December 31, 1999 and 1998 convertible subordinated debentures outstanding and related debt discount related to the following issuances are discussed below:

Issuance of debentures	December 31, 1999	December 31, 1998
	(in thousands)	
Debentures - August 1996 (a)	$ 2,500	$ 2,500
Debentures - March 1998 (b)	20,800	20,800
Debentures - issued in lieu of interest for March 1998 (b)	667	
Debentures - June 1998 (c)	5,000	5,000
Debentures - issued in lieu of interest for June 1998 (c)	158	
Debentures - May 1999 (d)	12,862	
Debentures - issued in lieu of interest for May 1999 (d)	114	
Debentures - July 1999 (e)	5,000	
	47,101	28,300
Less: Debt discount	(6,005)	(2,114)
	$ 41,096	$ 26,186

(a) On August 6, 1996, the Company issued 250 units, at $10,000 per unit, in a private placement of its securities ("August Private Placement"). Each unit consisted of: (i) a 10% convertible subordinated debenture due August 6, 2001 in the principal amount of $10,000, interest payable quarterly, and convertible into shares of the Company's common stock at a conversion price of $3.25 per share, subject to dilution, and (ii) 461 redeemable common stock purchase warrants ("warrants"). Each warrant entitled the holder to purchase one share of common stock for $3.25, subject to adjustment during the five-year period commencing August 6, 1996.

(b) On March 10, 1998, the Company completed a private offering (the "Offering") of securities to an investor group ("Galen") consisting of 5% convertible senior secured debentures due March 15, 2003, and common stock purchase warrants (with a 7 year life) exercisable for 2,244,667 shares of the Company's common stock at an exercise price of $1.404 and 2,189,511 shares at an exercise price of $2.279. The debentures are convertible into shares of the Company's common stock at a conversion price of $1.404. The net proceeds to the Company from the Offering, after the deduction of related offering expenses of $1,518,000 for legal and investment banker fees, was approximately $19,300,000. These related offering costs are being amortized over the remaining five year life of the related debentures.

NOTE G (CONTINUED)

(c) In accordance with the terms of the Offering, during June 1998, Galen invested an additional $5,000,000 in the Company in exchange for debentures and warrants having terms identical to those issued in the Offering (539,583 and 526,325 common stock purchase warrants with an exercise price of $1.404, respectively).

(d) On May 26, 1999, the Company consummated a private offering of securities for an aggregate purchase price of up to $22,800,000 (the "Oracle Offering"). The securities issued in the Oracle Offering consisted of 5% convertible senior secured debentures (the "1999 Debentures") and common stock purchase warrants (the "1999 Warrants"), each of which are substantially similar to the debentures and warrants issued by the Company in the Galen Offering completed in March, 1998. Of the $22,800,000 to be invested pursuant to the Oracle Offering, $5,000,000 was funded by Oracle Strategic Partners, L.P. ("Oracle") on May 26, 1999, the closing date of the Oracle Offering, with an additional $10,000,000 to be funded by Oracle in two installments of $5,000,000 each. The first $5,000,000 installment of the additional $10,000,000 Oracle investment was funded on July 27, 1999. Pursuant to an agreement reached between the Company and Oracle on March 20, 2000, the final $5,000,000 investment has been waived.

The 1999 Debentures were issued at par and will become due and payable as to principle on March 15, 2003. Approximately $12,800,000 in principle amount of the 1999 Debentures were issued on May 26, 1999. Interest on the principle of the 1999 Debentures is accrued at the rate of 5% per annum and is payable on a quarterly basis.

The 1999 Debentures are convertible into shares of the Company's common stock at a conversion price of $1.404 per share, for an aggregate of up to approximately 12,678,063 shares of the Company's common stock. The 1999 Warrants are exercisable for an aggregate of approximately 4,618,702 shares of the Company's common stock. Of such warrants, 2,309,351 warrants are exercisable at $1.404 per share and the remaining 2,309,351 warrants are exercisable at $2.279 per share. The 1999 Debentures and 1999 Warrants are convertible and exercisable, respectively, for an aggregate of approximately 17,296,765 shares of the Company's common stock.

NOTE G (CONTINUED)

(e) Approximately $7,037,000 of the 1999 Debentures issued pursuant to the Oracle Offering were issued in exchange for the surrender of a like amount of principal and accrued interest outstanding under the Company's convertible promissory notes issued pursuant to various bridge loan transactions with Galen Partners III, L.P., Galen Partners International III, L.P., Galen Employee Fund III, L.P. (collectively, "Galen") and certain other investors in the aggregate amount of $10,104,110 during the period from August 1998 through and including May, 1999 (the "1999 Galen Bridge Loans"). In exchange for Galen and other investors granting extensions to maturity dates of the Company's convertible promissory notes, the Company issued 1,022,284 common stock purchase warrants at exercise prices ranging from $1.18 to $2.32. These warrants resulted in deferred private offering costs which are being amortized over the remaining 5 year life of the related obligations. The remaining balance of the 1999 Galen Bridge Loans in the principal amount of $3,495,000 plus accrued and unpaid interest was paid on July 27, 1999.

(f) In connection with certain 1995 amendments to a line of credit agreement then existing with a bank, the Company issued stock warrants to the bank, expiring July 17, 2000, to purchase shares of the Company's common stock at various exercise prices per share, subject to certain antidilution provisions. At December 31, 1999 the number of common stock warrants, as adjusted, equal 955,509 shares at exercise prices ranging from $1.48 to $1.51 per share. In March 1998, the Company completely satisfied its bank indebtedness and terminated the line of credit agreement.

NOTE G (CONTINUED)

Debt discount resulting from the issuance of stock warrants in connection with the issuance of subordinated debt is recorded as a reduction of the related obligations at the warrants relative fair value and is amortized as additional interest expense over the remaining life of the related obligations. At December 31, 1999 outstanding warrants giving rise to debt discount for related debentures are as follows:

Warrants related to debentures above	Exercise prices	Number of Warrants	Original debt discount	Accumulated Amortization at December 31, 1999	Unamortized debt discount at December 31, 1999	Remaining life (months)
				(in thousands)		
(a)	$3.25	$ 115,250	$ 355	$ 237	$ 118	20
(b)	$1.404 and $2.279	4,434,178	2,263	793	1,470	39
(c)	$1.404 and $2.279	1,065,908	1,200	248	952	46
(d)	$1.404 and $2.279	3,608,604	4,034	569	3,465	39
(f)	$1.48 to $1.51	955,509	200	200	-	-
		$10,179,449	$8,052	$2,047	$6,005	

At December 31, 1999 outstanding warrants giving rise to deferred private offering costs are as follows:

Warrants	Exercise prices	Number of Warrants	Original deferred private issuance costs	Accumulated Amortization at December 31, 1999	Unamortized Private issuance costs at December 31, 1999	Remaining life (months)
				(in thousands)		
(e)	$1.18 to $2.32	$1,022,284	$ 907	$181	$726	48

NOTE H -NOTES PAYABLE

At December 31, 1999 and 1998, notes payable consisted of the following:

	December 31,	
	1999	1998
	(in thousands)	
Unsecured promissory demand notes (a)	$ 2,529	$ 2,817
Bridge Loans (b)	1,509	8,033
	$ 4,038	$10,850

(a) At December 31, 1999 unsecured promissory demand notes consisted of $2,379,000 due to Mylan and $150,000 due to a former employee. During the period from May 1997 through July 1997, the Company borrowed approximately $3 million from Mylan Laboratories, Inc. ("Mylan") pursuant to five unsecured, demand promissory notes. The advances made by Mylan Laboratories, Inc. were part of a proposed investment by Mylan in the Company, including the proposed purchase of the Company's Indiana facility as well as a partial tender offer for the Company's common stock. To date, $620,000 has been paid by the Company to Mylan against such indebtedness in the form of product deliveries to Mylan. Pursuant to an agreement reached between the parties, the Company is required to satisfy interest on the outstanding indebtedness on an annual basis while the indebtedness remains outstanding and to satisfy the principal amount of such indebtedness in the form of product deliveries to Mylan until such time as the indebtedness is satisfied in full.

(b) In addition to the 1999 Galen Bridge Loans discussed in Note G, the Company secured bridge financing from Galen order to provide necessary working capital prior to the completion of the Watson Term Loan as described in Note Q. These bridge loans aggregated approximately $3,300,000 and were funded through six separate bridge loan transactions during the period from December 8, 1999 through March 29, 2000 (collectively, the "2000 Galen Bridge Loans"). At December 31, 1999 $1,509,000 relating to such bridge loans was outstanding. On March 31, 1999 the total principal amount of the 2000 Galen Bridge Loans and accrued and unpaid interest were satisfied in full with a portion of the proceeds of the Watson Term. Prior to repayment, the 2000 Galen Bridge Loans accrued interest at the rate of 18% per annum and were secured by a first lien on all of the Company's assets. In consideration for the extension of the 2000 Galen Bridge Loans, the Company issued common stock purchase warrants to Galen to purchase an aggregate of 125,000 shares of the Company's common stock.

NOTE H (CONTINUED)

The warrants issued pursuant to the 2000 Galen Bridge Loans have an exercise price equal to the fair market value of the Company's common stock on the date of issuance and are substantially identical to those issued by the Company in the Oracle Offering (Note G).

NOTE I- INCOME TAXES

The actual income tax expense varies from the Federal statutory rate applied to consolidated operations as follows:

	Year ended December 31,					
	1999		1998		1997	
	AMOUNT	%	Amount	%	Amount	%
			(in thousands)			
Federal statutory rate	$(6,116)	(34%)	$(4,326)	(34.0)%	$(5,105)	(34.0)%
Loss for which no tax benefit was provided	5,997	33.8%	4,247	33.8	4,924	32.8
Losses of subsidiaries with no tax benefit						
Amortization of warrants					24	.2
Goodwill amortization					12	.1
Department of Justice settlement	31	.1	42	.1		
Other	88	.1	37	.1	145	.9
Actual tax expense	$ --	--%	$ --	--%	$ --	--%

The Company has net operating loss carryforwards aggregating approximately $58,796,146, expiring during the years 2011 through 2019. In addition, certain of the Company's subsidiaries filed separate Federal income tax returns in prior years and have separate net operating loss carryforwards aggregating approximately $4,062,758 expiring during the years 1999 through 2018.

NOTE I (CONTINUED)

The tax loss carryforwards of the Company and its subsidiaries are subject to limitation by Section 382 of the Internal Revenue Code with respect to the amount utilizable each year. This limitation reduces the Company's ability to utilize net operating loss carryforwards included above each year. The amount of the limitation has not been quantified by the Company.

The components of the Company's deferred tax assets (liabilities), pursuant to SFAS No. 109, are summarized as follows:

	December 31,	
	1999	1998
	(in thousands)	
Deferred tax assets		
Net operating loss carryforwards	$ 27,349	$ 21,831
Allowance for doubtful accounts	50	75
Research and development tax credit	212	212
Reserve for inventory	218	169
Reserve for chargebacks	21	
Shutdown costs	1,352	
Severance package	242	
Litigation settlement	44	73
Rent	44	231
Reserve for Medicaid	93	71
Capital loss carryforwards	210	
Reserve for contingencies	14	
Charitable contribution carryforwards	1	
Other	26	15
Gross deferred tax assets	29,876	22,677
Deferred tax liabilities		
Depreciation	(430)	(332)
Installment sale gain		
Other	(42)	(42)
	(472)	(374)
Net deferred tax assets before valuation allowance	29,404	22,303
Valuation allowance	(29,404)	(22,303)
Net deferred tax assets	$ --	$ --

NOTE I (CONTINUED)

SFAS No. 109 requires a valuation allowance against deferred tax assets if, based on the weight of available evidence, it is more likely than not that some or all of the deferred tax assets may not be realized. The valuation allowance at December 31, 1999 primarily pertains to uncertainties with respect to future utilization of net operating loss carryforwards.

NOTE J - CESSATION AND RELOCATION OF BROOKLYN, NY PLANT OPERATIONS

The Company's formal decision to discontinue its Brooklyn operations was initiated in the fourth quarter of 1999 with notification to its union. The total charge of approximately $3,220,000 resulting from eliminating the Brooklyn operation includes the lease termination payment of $1,150,000, a provision of $200,000 for plant repairs, the write-off of leasehold improvements of $1,778,000, severance and other costs for terminated employees of $730,000, less deferred rent previously expensed of $638,000.

At December 31, 1999 the Company was obligated to pay rent through December 31, 2005 pursuant to a noncancellable lease obligation for its facility in Brooklyn, New York. Under a termination and settlement agreement consummated on March 22, 2000 (the "Settlement Agreement"), in exchange for a termination payment of $1,150,000, the termination of the lease has been accelerated to August 31, 2000. The total base rent payments that would have been required from September 1, 2000 to December 31, 2005, were approximately $6,715,000. The agreement does allow the Company to continue to lease the facility beyond August 31, 2000, but requires the Company to vacate the premises no later than March 31, 2001. In addition, the Settlement agreement provides for the advance payment of rent through August 31, 2000 and a restoration escrow deposit of $200,000 for plant repairs. The Company also deposited in escrow with its counsel $390,600 which represents rental payments for the period September 1, 2000 through March 31, 2001. Such escrow amount will be returned to the Company in the event it vacates the Brooklyn facility on or prior to August 31, 2000. The Company funded the termination fee payment, the advance rental payment obligations and restoration amount required pursuant to the Settlement Agreement with the proceeds received from the Watson Term Loan (Note Q).

NOTE K - SALE AND ACQUISITION OF ABBREVIATED NEW DRUG APPLICATIONS ("ANDA")

Sale of ANDA

On March 21, 1995, the Company sold its ANDA for 5mg Oxycodone HCL/325mg Acetaminophen Tablets ("Tablets") and certain equipment used in the production of the tablets. Pursuant to the agreement the Company recognized the final portion of the gain, $1,900,000, as other income in March 1998.

Acquisition of Barr Laboratories, Inc. ANDA

On April 16, 1999, the Company completed an acquisition agreement with Barr Laboratories, Inc. ("Barr") providing for the Company's purchase of the rights to 50 pharmaceutical products (the "Barr Products"). Under the terms of the acquisition agreement with Barr, the Company acquired all of Barr's rights in the Barr Products, including all related governmental approvals (including ANDAs) and related technical data and information. In consideration for the acquisition of the Barr Products, the Company issued to Barr a common stock purchase warrant exercisable for 500,000 shares of the Company's common stock having an exercise price of $1.0625 per share (the fair value of the Common Stock on the date of issuance) and having a term of five years. The Company valued the warrants at $350,000 using the Black Scholes option pricing model. Accordingly, the Company recorded a deferred charge to be amortized as an expense to the Company's operations over a 10 year period which is the estimated life of the related ANDA. The acquisition agreement with Barr also allows Barr to purchase any of the Barr Products manufactured by the Company for a period of five years.

NOTE L - PENSION EXPENSE

1. Management Pension Plan

The Company had maintained a defined benefit plan covering substantially all nonunion employees which was terminated in November 1996. Subsequently, all Plan assets were converted to cash and held in a money market fund (to continue the Trust) from which all vested participant interests were to be paid. In 1998, the Company received approval to terminate the Plan by the Pension Benefit Guarantee Corporation, all assets were distributed to the vested participants, the Trust was terminated and a final filing was made with the Internal Revenue Service.

NOTE L (CONTINUED)

2. Employees' Pension Plan

The Company contributed approximately $67,872, $421,000, and $407,000, in 1999, 1998 and 1997, respectively, to a multiemployer pension plan for employees covered by collective bargaining agreements. This plan is not administered by the Company and contributions are determined in accordance with provisions of negotiated labor contracts. Information with respect to the Company's proportionate share of the excess, if any, of the actuarially computed value of vested benefits over the total of the pension plan's net assets is not available from the plan's administrator.

The Multiemployer Pension Plan Amendments Act of 1980 (the "Act") significantly increased the pension responsibilities of participating employers. Under the provision of the Act, if the plans terminate or the Company withdraws, the Company could be subject to a "withdrawal liability."

NOTE M - STOCK OPTION PLAN

In June 1998, the stockholders of the Company approved the adoption of a stock option and restricted stock purchase plan (the "1998 Option Plan). The 1998 Option Plan provides for the granting of (i) nonqualified options to purchase the Company's common stock at not less than the fair market value on the date of the option grant and (ii) incentive stock options to purchase the Company's common stock at not less than the fair market value on the date of the option grant. As of December 31, 1999, there was no exercise of any options to purchase any common stock under the 1998 Option Plan. The total number of shares which may be sold pursuant to options and rights granted under the 1998 Option Plan is 3,600,000. No option can be granted under the 1998 Option Plan after April, 2008 and no option can be outstanding for more than ten years after its grant.

The Company has adopted the disclosure provisions of Statement of Financial Accounting Standards No. 123 ("SFAS No. 123"), "Accounting for Stock-Based Compensation." It applies APB Opinion No. 25, "Accounting for Stock Issued to Employees," and related interpretations in accounting for its plans and does not recognize compensation expense for its stock-based compensation plans other than for restricted stock. If the Company had elected to recognize compensation expense based upon the fair value at the grant date for awards under these plans consistent with the methodology prescribed by SFAS No. 123, the Company's net income and earnings per share would be reduced to the pro forma amounts indicated below:

NOTE M (CONTINUED)

	Year ended December 31,		
	1999	1998	1997
	(thousands, except per share amounts)		
Net loss			
As reported	$ (20,063)	$ (12,724)	$ (15,013)
Pro forma	(20,954)	(13,663)	(15,323)
Loss per share			
As reported	$ (1.40)	$ (.92)	$ (1.12)
Pro forma	(1.46)	(.98)	(1.14)

These pro forma amounts may not be representative of future disclosures because they do not take into effect pro forma compensation expenses related to grants made before 1995. The fair value of these options was estimated at the date of grant using the Black-Scholes option-pricing model with the following weighted average assumptions for the years ended December 31, 1999, 1998 and 1997, respectively: expected volatility of 73%, 67%, and 65%; risk-free interest rates of 6.8%, 5.6%, and 6.0%; and expected lives of 10 years, 10 years, and 4 years. At the date of grant, all exercise prices equaled the market value of the stock.

The Black-Scholes option valuation model was developed for use in estimating the fair value of traded options which have no vesting restrictions and are fully transferable. In addition, option valuation models require the input of highly subjective assumptions including the expected stock price volatility. Because the Company's employee stock options have characteristics significantly different from those of traded options, and because changes in the subjective input assumptions can materially affect the fair market estimate, in management's opinion, the existing models do not necessarily provide a reliable single measure of the fair value of its employee stock options.

NOTE M (CONTINUED)

Transactions involving stock options are summarized as follows:

	Stock options outstanding	Weighted average exercise Price	Weighted average fair value
Balance at December 31, 1996	656,007	3.53	
Exercised	(89,300)	3.22	$3.39
Cancelled	(84,968)	5.16	3.39
Balance at December 31, 1997	481,739	3.60	
Granted	2,254,850	2.37	1.71
Cancelled	(511,303)	3.16	2.08
Balance at December 31, 1998	2,225,286	2.46	
Granted	503,500	1.19	.80
Cancelled	(118,567)	3.08	2.00
Balance at December 31, 1999	2,610,219	2.19	

The following table summarizes information concerning currently outstanding and exercisable stock options:

	Options outstanding			Options exercisable	
Ranges of exercise prices	Number outstanding at December 31, 1999	Weighted average remaining contractual Life(years)	Weighted average exercise price	Number exercisable at December 31, 1999	Weighted average exercise price
$1.00 - $2.00	518,100	9.09	$1.17	86,250	$1.30
2.01 - 3.00	2,023,850	8.21	2.40	918,463	2.39
3.01 - 4.88	68,269	6.23	3.78	62,019	3.64
	2,610,219			1,066,732	

NOTE N - COMMITMENTS

The Company occupies plant and office facilities under noncancellable operating leases which expire in December 2005. These operating leases provide for scheduled base rent increases over the term of the lease, however, the total amount of the base rent payments will be charged to operations using the straight-line method over the term of the lease. The leases provide for payment of real estate taxes based upon a percentage of the annual increase. In addition, the Company rents certain equipment under operating leases, generally for terms of four years. Total rent expense for the years ended December 31, 1999, 1998 and 1997 was approximately $1,574,000, $1,243,000, $884,000, respectively. See Note J for information relating to the shutdown of the Brooklyn, New York facility.

Lease of Congers, New York Facility

Effective March 22, 1999, the Company leased, as sole tenant, a pharmaceutical manufacturing facility located in Congers, New York (the "Congers Facility") from Par Pharmaceutical, Inc. ("Par") pursuant to an Agreement to Lease (the "Lease"). The Congers Facility contains office, warehouse and manufacturing space. The Lease provides for a term of three years, with a two-year renewal option and provides for annual fixed rent of $500,000 per year during the primary term of the Lease and $600,000 per year during the option period. The Lease also covers certain manufacturing and related equipment previously used by Par in its operations at the Congers Facility (the "Leased Equipment"). In connection with the execution of the Lease, the Company and Par entered into a certain Option Agreement pursuant to which the Company may purchase the Congers Facility and the Leased Equipment at any time during the lease term for $5,000,000.

As part of the execution of the Lease, the Company and Par entered into a certain Manufacturing and Supply Agreement (the "M&S Agreement") having a term of two years. The M&S Agreement provides for the Company's contract manufacture of certain designated products. The M&S Agreement also provides that Par will purchase a minimum of $1,150,000 in product during the initial 18 months of the Agreement. The M&S Agreement further provides that the Company will not manufacture, supply, develop or distribute the designated products to be supplied by the Company to Par under the M&S Agreement to or for any other person for a period of three years.

NOTE N (CONTINUED)

As of December 31, 1999, the approximate minimum rental commitments under these operating leases are as follows:

Twelve months ending December 31,	(in thousands)
2000	$1,360
2001	509
2002	104
2003 and thereafter	7
Total minimum payments required	$1,980

Employment Contracts

During March 1998, the Company entered into employment contracts with each of two new officers/employees of the Company which cover a five-year and a three-year period, respectively. The contracts provide for, among other things: (i) annual salaries of $170,000 and $140,000 to be paid over the five-year and three-year periods, respectively and (ii) an aggregate of 1,300,000 options (included in the 1998 grants - Note M) to purchase the Company's stock at an exercise price of $2.38 per common share that vest evenly over a three-to-five-year service period and expire in ten years.

NOTE O - CONTINGENCIES

American Stock Exchange

The Company has been advised by the American Stock Exchange ("Amex") that the Amex has determined to delist the Common Stock of the Company (stock symbol "HDG") as it does not meet the Amex's criteria for continued listing. Such criteria include minimum levels of shareholders' equity and the absence of years of net losses from continuing operations. In response to the Amex notice, the Company has exercised its right to appeal the Amex's decision and has requested a formal hearing in order to further consider the decision. There can be no assurance that the Company's common stock will remain listed on the Amex. In the event the Company is unsuccessful in its appeal to maintain the listing of the Company's Common Stock on the Amex, it is anticipated that the Company's Common Stock will trade on the Over the Counter Bulletin Board. In such event, a shareholder may find it more difficult to dispose of, or to obtain accurate quotations as to the market value of the Common Stock.

NOTE O (CONTINUED)

Department of Justice ("DOJ") Settlement

On June 21, 1993, the Company entered into a Plea Agreement with the DOJ to resolve the DOJ's investigation into the manufacturing and record keeping practices of the Company's Brooklyn plant. The Plea Agreement required the Company to pay a fine of $2,500,000 over five years in quarterly installments of $125,000, commencing on or about September 15, 1993.

As of February 28, 1998, the Company was in default of the payment terms of the Plea Agreement and had made payments aggregating $350,000. On March 27, 1998, the Company and the DOJ signed the Letter Agreement serving to amend the Plea Agreement relating to the terms of the Company's satisfaction of the fine assessed under the Plea Agreement. Specifically, the Letter Agreement provided that the Company will satisfy the remaining $2,150,000 of the fine through the payment of $25,000 on a monthly basis commencing June 1, 1998, plus interest on such outstanding balance (at the rate calculated pursuant to 28 U.S.C Section 1961)(currently 5.319%). Such payment schedule will result in the full satisfaction of the DOJ fine in December, 2005. The Letter Agreement also provides certain restrictions on the payment of salary or compensation to any individual in excess of $150,000 without the written consent of the DOJ. In addition, the Letter Agreement requires the repayment of the outstanding fine to the extent of 25% of the Company's after-tax profit or the remaining balance owed and 25% of the net proceeds received by the Company on any sale of a capital asset for a sum in excess of $10,000. At December 31, 1999, the Company is current in its payment obligations with a remaining obligation of $1,675,000.

Other Legal Proceedings

Beginning in 1992, actions were commenced against the Company and numerous other pharmaceutical manufacturers in the Pennsylvania Court of Common Pleas, Philadelphia Division, in connection with the alleged exposure to diethylstilbestrol ("DES"). The defense of all of such matters was assumed by the Company's insurance carrier, and a substantial number have been settled by the carrier. Currently, several actions remain pending with the Company as a defendant, and the insurance carrier is defending each action. Similar actions were brought in Ohio, and have been dismissed based on Ohio law. The Company and its legal counsel do not believe any of such actions will have a material impact on the Company's financial condition. The ultimate outcome of these lawsuits cannot be determined at this time, and accordingly, no adjustment has been made to the consolidated financial statements.

NOTE O (CONTINUED)

The Company has been named as a defendant in one additional action which has been referred to the Company's carrier and has been accepted for defense. This action, Alonzo v. Halsey Drug Co., Inc. and K-Mart Corp. was commenced on November 5, 1995 and involves a claim for unspecified damages relating to the alleged ingestion of "Doxycycline 100." The ultimate outcome of these lawsuits cannot be determined at this time, and accordingly, no adjustment has been made to the consolidated financial statements.

NOTE P - SIGNIFICANT CUSTOMERS AND SUPPLIERS

The Company sells its products to a large number of customers who are primarily drug distributors, drugstore chains and wholesalers and are not concentrated in any specific region. The Company performs ongoing credit evaluations of its customers and generally does not require collateral. During 1999, the Company had net sales to one customer in excess of 10% of total sales, aggregating 16.3% of total sales. During 1998, the Company had net sales to one customer in excess of 10% of total sales, accounting for 17.6% of total sales. During 1997, the Company had net sales to one customer in excess of 10% of total sales, aggregating 22.3% of total sales.

During 1999 and 1998, the Company purchased approximately $1,107,000 and $2,583,000, respectively, of its raw materials, representing approximately 15% and 29%, respectively, of total raw material purchases from one supplier.

NOTE Q - SUBSEQUENT EVENT - STRATEGIC ALLIANCE WITH WATSON PHARMACEUTICALS

On March 29, 2000, the Company 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, for Watson's marketing and sale of the Company's core products and for Watson's extension of a $17,500,000 term loan to the Company.

NOTE Q (CONTINUED)

The product acquisition portion of the transactions with Watson provided for Halsey's sale of a pending ANDA and related rights (the "Product") to Watson for aggregate consideration of $13,500,000 (the "Product Acquisition Agreement"). 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. Management expects the last of these milestones to be achieved by no later than the end of the second fiscal quarter of year 2000.

The Company and Watson also 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 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 other APIs or finished dosage products for itself or third parties.

The Company and Watson also completed 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

NOTE Q (CONTINUED)

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, including, without limitation, the Product sold to Watson, and the marketing and sale of same, of which there can be no assurance, substantially all the Company's revenues expect to 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 advance. 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.

Exhibit 3.1

CERTIFICATE OF AMENDMENT

OF THE CERTIFICATE OF INCORPORATION

OF

HALSEY DRUG CO., INC.

UNDER SECTION 805 OF THE NEW YORK BUSINESS CORPORATION LAW

* * * * *

WE, THE UNDERSIGNED, Michael K. Reicher and Peter Clemens, being respectively the President and the Secretary of Halsey Drug Co., Inc., hereby certify:

1. The name of the corporation is Halsey Drug Co., Inc. The corporation was originally incorporated under the name of Halsey Drug Co. Inc.

2. The certificate of incorporation of said corporation was filed with the Department of State on the 10th day of April, 1935, and has been amended at various times by action of the Board of Directors and the shareholders of the corporation.

3. (a) The Certificate of Incorporation is amended to (i) increase the number of authorized shares of common stock from 40,000,000 to 80,000,000 shares, (ii) increase the number of directors to not more than eleven (11) and (iii) grant voting rights on an as-converted basis to the holders of the Company's 5% Convertible Senior Secured Debentures due March 15, 2003 issued pursuant to that certain Debenture and Warrant Purchase Agreement dated May 26, 1999 between the Corporation, Oracle Strategic Partners, L.P. and the other signatories thereto.

(b) To effect the foregoing, the following amendments are hereby made to the corporation's certificate of incorporation, as amended:

(A) Article THIRD relating to the amount of authorized capital stock of the corporation is amended to read as follows:

THIRD: The amount of the authorized capital stock of the Corporation shall be Eight Hundred Thousand ($800,000) Dollars consisting of 80,000,000 shares of Common Stock, each share having a par value of $.01 per share.

The holders of the Corporation's 5% Convertible Senior Secured Debentures due March 15, 2003 originally issued pursuant to that certain Debenture and Warrant Purchase Agreement dated March 10, 1998 between the Corporation, Galen Partners III, L.P., Galen Partners International, L.P., Galen Employee Fund, III, L.P., and each of the other signatories thereto (the "1998 Debentures") and the holders of the Corporation's 5% Convertible Senior Secured Debentures due March 15, 2003 originally issued pursuant to that certain Debenture and Warrant Purchase Agreement dated May 26, 1999 between the Corporation, Oracle Strategic Partners, L.P. and each of the other signatories thereto (the "1999 Debentures" and together with the 1998 Debentures, collectively, the "Debentures"), shall be entitled to vote on all matters submitted to a vote of the shareholders of the Corporation, together with the holders of the Corporation's Common Stock (and any other shares of capital stock of the Corporation entitled to vote at a meeting of shareholders) as one class. Each Debenture shall be entitled to a number of votes equal to the number of votes represented by the Common Stock of the Corporation that could then be acquired upon conversion of the Debentures into Common Stock, subject to adjustments as provided in the Debentures. Holders of the Debentures shall be deemed to be shareholders of the Corporation, and the Debentures shall be deemed to be shares of stock for purposes of any provision of the New York Business Corporation Law that requires the vote of shareholders as a prerequisite to any corporate action.

(B) ARTICLE SIXTH relating to the number of directors is amended to read as follows:

SIXTH: The number of directors shall be not less

than three (3) nor more than eleven (11), none of whom need be stockholders of the Corporation.

4. The amendments provided herein were authorized in the following manner:

By the unanimous written consent of the Board of Directors followed by an affirmative vote of the holders of a majority of the outstanding shares of Common Stock of the Corporation entitled to vote thereon.

IN WITNESS WHEREOF, we have signed this certificate on the 19th day of August 1999 and we affirm the statements contained herein as true under penalties of perjury.

/s/ Michael K. Reicher

Michael K. Reicher
President and Chief Executive Officer

/s/ Peter Clemens

Peter Clemens
Secretary

Exhibit 10.72

May 26, 1999

To the Purchaser(s) Set Forth on Exhibit A hereto:

HALSEY DRUG CO., INC., a New York corporation (the "Company"), agrees with you as follows:

ARTICLE I

AUTHORIZATION OF THE SECURITIES; ADJUSTMENT OF CONVERSION PRICE AND WARRANT PRICES

I.1. Authorization of Securities. The Company represents that it has taken all corporate action necessary to authorize the issuance and sale of (a) its 5% Convertible Senior Secured Debentures due March 15, 2003 in the aggregate principal amount of $22,862,603.04 (the "Debentures"), (b) warrants to purchase an aggregate of 2,309,351 shares of Common Stock, par value $.01 per share ("Common Stock"), of the Company initially at a price of $1.404 per share (the "$1.404 Warrants") and (c) warrants to purchase an aggregate of 2,309,351 shares of Common Stock initially at a price of $2.285 per share (the "$1.404 Warrants" and together with the $2.285 Warrants, the "Warrants"). The Debentures and the Warrants (collectively, the "Securities") are to be sold pursuant to this Agreement to you (each of you is sometimes referred to herein as a "Purchaser"). Interest on the Debentures is payable at the rate of 5% per annum, as more particularly specified in the form of Debenture attached hereto as Exhibit B. Each Debenture is convertible in whole or in part from time to time into a number of shares of Common Stock initially at the rate of one share of Common Stock for each $1.404 in principal amount of the Debenture to be converted. For purposes of this Agreement, the term "Shares" shall mean the shares of Common Stock which may be issued upon conversion of all or a portion of the principal amount of the Debentures and the shares of Common Stock that may be issued from time to time pursuant to the exercise of the Warrants. The term "Shares" does not include any other shares of Common Stock or other capital stock of the Company.

I.2. Adjustment of Conversion Price and Warrant Prices. The prices at which Shares may be acquired upon conversion of the Debentures and exercise of the Warrants (the "Conversion Price" and the "Warrant Prices", respectively) are subject to adjustment as set forth therein.

ARTICLE II

SALE AND PURCHASE OF THE SECURITIES; SECURITY DOCUMENTS

II.1. Sale and Purchase of the Securities. Subject to the terms and conditions hereof and in reliance on the representations and warranties contained herein, or made pursuant hereto, the Company will issue and sell to each Purchaser and/or such Purchaser's designees, and each Purchaser, severally and not jointly, will purchase from the Company, on the Closing Date specified in Article 3, the Securities for the purchase prices set forth opposite such Purchaser's name on Exhibit A.

The Company and Oracle Strategic Partners, L.P. ("Oracle") acknowledge and agree that the funding of the remaining aggregate of $10,000,000 in principal amount of the Debentures as set forth in Exhibit A hereto will be funded in two (2) equal installments (each an Installment"). The first Installment of $5,000,000 will be made within three (3) business days after the later to occur of (i) written notice by the Company to Oracle of the Company's receipt of approval from the U.S. Food and Drug Administration ("FDA") relating to its Abbreviated New Drug Application ("ANDA") for Prednisolone Syrup, and (ii) written notice by the Company to Oracle indicating that the Charter Amendment (as defined and provided in Section 9.12(B) hereof) has been filed with, and accepted for filing by, the Office of the Department of State of the State of New York (such notice shall include a copy of the Charter Amendment stamped "filed" by the Office of the Department of State of the of New York). The second and final Installment of $5,000,000 will be funded within three (3) business days after the later of: (i) written notice by the Company to Oracle of the Company's receipt of FDA approval for the ANDA relating to Doxycycline Monohydrate; (ii) receipt of shareholder approval of the proposals as described in Section 9.12(B) hereof, provided, however that in the event that FDA approval of the ANDA relating to Doxycycline Monohydrate shall not have been received on or prior to March 31, 2000, Oracle shall have no obligation to fund the final $5,000,000 Installment as provided herein and in Exhibit A hereto. The Company shall provide Oracle with written evidence of the FDA's approval of the ANDA for each of Prednisolone Syrup and Doxycycline Monohydrate promptly upon receipt of same from the FDA.

II.2. Company Security Documents. All of the obligations of the Company under the Debentures shall be secured by the following:

(a) A lien on all the personal property and assets of the Company now existing or hereinafter acquired granted pursuant to a Company General Security Agreement dated of even date herewith between the Company and Oracle, as agent for the Purchasers (the "Company General Security Agreement"), which, except for Permitted Liens (as hereinafter defined in Section 10.4), shall be a first lien ranking pari passu with the lien granted to the investors in the Company's 5% convertible senior secured debentures due March 15, 2003 issued pursuant to a certain Debenture and Warrant Purchase Agreement dated March 10, 1998 between the Company and the Purchasers listed on the signature page thereto (the "March 1998

Debentures").

(b) Collateral assignments of all leases, contracts, patents, copyrights, trademarks and service marks of the Company (collectively, the "Company Collateral Assignments").

II.3. Guaranties. All of the obligations of the Company under the Debentures shall be guaranteed pursuant to Continuing Unconditional Secured Guaranties (each, a "Guaranty" and collectively, the "Guaranties") by each of the following subsidiaries of the Company (each, a "Guarantor"):

(a) Houba, Inc. ("Houba"); and
(b) Halsey Pharmaceuticals, Inc.

II.4. Guarantor Security Documents. All of the obligations of the Guarantors under the Guaranties shall be secured by the following:

(a) A lien on all of the personal property and assets of the respective Guarantors now existing or hereinafter acquired, granted pursuant to a Guarantors General Security Agreement dated of even date herewith between the Guarantors and Oracle, as agent for the Purchasers (the "Guarantors Security Agreement"), which, except for Permitted Liens (as hereinafter defined in Section 10.4), shall be a first lien ranking pari passu with the lien granted to the investors in the March 1998 Debentures.

(b) Collateral assignments of all leases, contracts, patents, copyrights, trademarks and service marks of the Guarantors (collectively, "Guarantor Collateral Assignments").

(c) A first mortgage granted by Houba on real property owned by Houba located at 16235 State Road 17, Culver, Indiana (the "Mortgage").

ARTICLE III

CLOSING

The closing of the purchase and sale of the Securities (the "Closing") will take place at the offices of St. John & Wayne, Two Penn Plaza East, Newark, New Jersey 07105 simultaneously with the execution of this Agreement, or such other place, time and date as shall be mutually agreed to by the Company and the Purchasers. Such time and date is herein called the "Closing Date."

On the Closing Date there will be delivered to each Purchaser: (a) a Debenture dated the Closing Date, in the principal amount set forth opposite the name of such Purchaser in Exhibit A, (b) a warrant certificate or certificates substantially in the form of Exhibit C registered in such Purchaser's name representing the right to purchase for $1.404 per Share the number of Shares set forth opposite the name of such Purchaser on Exhibit A and (c) a warrant certificate or certificates substantially in the form of Exhibit D representing the right to purchase for $2.285 per Share the number of Shares set forth opposite the name of such Purchaser on Exhibit A. The number of Shares which may be purchased upon exercise of the Warrants is subject to adjustment as provided therein. The foregoing Securities shall be delivered by the Company, against delivery by each Purchaser to the Company of a certified or official bank check payable to the order of the Company drawn upon or issued by a bank which is a member of the New York Clearinghouse for banks (or wire transfer) for the amount set forth opposite the name of such Purchaser on Exhibit A.

ARTICLE IV

REPRESENTATIONS AND WARRANTIES OF THE COMPANY

The Company represents and warrants to you as follows:

IV.1. Organization and Existence, etc. Except as set forth in Section 4.1 of the Schedule of Exceptions attached hereto as Exhibit E (the "Schedule of Exceptions") or in the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 1998 (the "Annual Report"), the Company is a corporation duly organized and validly existing and in good standing under the laws of its jurisdiction of incorporation and is qualified to do business in such other jurisdictions as the nature of its operations or the ownership of its properties require such qualification, except where the failure to be so qualified could not reasonably be expected to have a material adverse effect on the Company's business, operations, assets or condition (financial or otherwise), or on its ability to perform its obligations under this Agreement and the transactions contemplated hereby (a "Material Adverse Effect") and has all requisite corporate power and authority to carry on its business as now conducted and proposed to be conducted; the Company has all requisite corporate power and authority to enter into this Agreement, to issue the Securities as contemplated herein and to carry out and perform its obligations under the terms and conditions of this Agreement. The Company 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 could reasonably be expected to have a Material Adverse Effect or subject the Company to a material liability. The Company has furnished Purchasers with true, correct and complete copies of its Certificate of Incorporation, By-Laws and all amendments thereto, as of the date hereof.

IV.2. Subsidiaries and Affiliates. Section 4.2 of the Schedule of Exceptions sets forth the name, jurisdiction of incorporation and authorized and outstanding capitalization of each entity in which the Company 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 4.2 of the Schedule of Exceptions, the Company has, and upon the Closing will have, no Subsidiaries and 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 4.2 of the Schedule of Exceptions or in the Annual Report, 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 4.2 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 could reasonably be expected to have a Material Adverse Effect on the Company and its Subsidiaries, taken as a whole, or subject such Subsidiary to a material liability.

IV.3. Capitalization.

(a) As of the date hereof, the Company's authorized capital stock consists of 40,000,000 shares of Common Stock, par value $.01 per share, of which 14,286,440 shares are outstanding and 25,713,560 are reserved for issuance for the purposes set forth in Section 4.3 of the Schedule of Exceptions. As of the date hereof, the Company 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 Company 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 Company in compliance with applicable Federal and state securities laws. Other than as set forth in Section 4.3(a), Section 4.3 of the Schedule of Exceptions or the Annual Report, there are no outstanding preemptive, conversion or other rights, options, warrants, calls, agreements or commitments granted or issued by or binding upon the Company, for the purchase or acquisition of any shares of its capital stock or securities convertible into or exercisable or exchangeable for capital stock.

IV.4. Authorization. All corporate action on the part of the Company and the directors and, except as otherwise provided in Section 9.12 hereof, stockholders of the Company necessary for the authorization, execution, delivery and performance by the Company of this Agreement and the transactions contemplated herein, and for the authorization, issuance and delivery of the Securities, has been taken or will have been taken prior to the Closing.

IV.5. Binding Obligations; No Material Adverse Contracts, etc. This Agreement is a valid and binding obligation of the Company enforceable in accordance with its terms. Except as set forth in Section 4.5 of the Schedule of Exceptions and as provided in Sections 9.12 and 9.14 hereof, the execution, delivery and performance by the Company of this 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 Company is subject, the Certificate of Incorporation, as amended, or the By-Laws, as amended, of the Company, or any mortgage, indenture, agreement, instrument, judgment, decree, order, rule or regulation or other restriction to which the Company is a party or by which it is bound, which violation or conflict could reasonably be expected to have a Material Adverse Effect, or except for liens on the assets of the Company created in favor of the Purchasers and the investors in the March 1998 Debentures, result in the creation of any mortgage, pledge, lien, encumbrance or charge upon any of the properties or assets of the Company pursuant to any such term. Except as set forth in Section 4.5 of the Schedule of Exceptions or the Annual Report, no stockholder of the Company has or will have any preemptive rights or rights of first refusal by reason of the issuance of the Securities or Shares issuable upon conversion or exercise of the Securities.

IV.6. Compliance with Instruments, etc. Except as set forth in Section 4.6 of the Schedule of Exceptions or the Annual Report, neither the Company 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 could reasonably be expected to have a Material Adverse Effect on the Company and its Subsidiaries taken as a whole.

IV.7. Litigation. Except as set forth in Section 4.7 of the Schedule of Exceptions or the Annual Report, there is no action, suit or proceeding pending, or, to the knowledge of the Company, threatened, against the Company or any Subsidiary before any court, administrative agency or arbitrator or any action, suit or proceeding pending, or, to the knowledge of the Company, threatened, which challenges the validity of any action taken or to be taken pursuant to or in connection with this Agreement or the issuance of the Securities.

IV.8. Financial Information; SEC Documents.

(a) The Company has furnished to the Purchasers the consolidated financial statements of the Company 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 the Company's Annual Report on Form 10-K for the year ended December 31, 1998 filed with the Securities and Exchange Commission (the "Commission") under the Securities Exchange Act of 1934, as amended (the "Exchange Act"). Such financial statements fairly present the condition of the Company and its Subsidiaries as of the dates thereof and the results of the operations of the Company and its Subsidiaries for such periods.

(b) The Company has also furnished to the Purchasers the unaudited consolidated balance sheet of the Company and its subsidiaries as of March 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 ended March 31, 1999 and March 31, 1998. Such financial statements fairly present, in conformity with 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 the Company and its Subsidiaries as of such date and their consolidated results of operations for such periods (subject to normal year-end adjustments)

(c) None of the documents filed by the Company with the Commission since December 31, 1997 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 Company which the Company has not disclosed to the Purchasers prior to or as of the date of this 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 Company and its Subsidiaries, taken as a whole.

IV.9. Offering. Subject in part to the truth and accuracy of the Purchasers' representations and the compliance by each Purchaser with its covenants set forth in this Agreement and any subscription agreement executed and delivered by the Purchasers, the offer, sale and issuance of the Securities as contemplated by this Agreement are not subject to the registration requirements of the Securities Act of 1933, as amended (the "Securities Act"), and the Company, or anyone acting on its behalf, will not take any action hereafter that would cause such registration requirements to be applicable.

IV.10. Permits; Governmental and Other Approvals.

(a) Other than as set forth in Section 4.10 of the Schedule of Exceptions or the Annual Report, each of the Company 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 could not reasonably be expected to have a Material Adverse Effect on the Company and its Subsidiaries taken as a whole) and the Company and its Subsidiaries are not in default under any of such franchises, licenses, permits or other authority. Other than as set forth in Section 4.10 of the Schedule of Exceptions, the Annual Report or as otherwise contemplated in Article IX hereof, 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 Company's valid execution, delivery and performance of this Agreement or the offer, issuance and sale of the Securities by the Company to the Purchasers or the consummation of any other transaction contemplated on the part of the Company hereby.

(b) Without limiting the generality of the representations and warranties made in Section 4.10(a), the Company represents and warrants that (i) it and the Guarantors 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 the Guarantors are not adulterated or misbranded and are in lawful distribution, and (iii) it and the Guarantors are in compliance with the following specific requirements: the Company and the Guarantors have registered all facilities with the United States Food and Drug Administration (the "FDA"); the Company and the Guarantors have listed all drug products with the FDA; each drug product marketed by the Company or any Guarantor 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 Company and the Guarantors is in compliance in all material respects with the terms of the consent agreement entered into by the Company with the United States Attorney for the Eastern District of New York on behalf of the FDA on June 29, 1993, as amended; to the Company's knowledge, neither the Company nor any Guarantor 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 Company or a Guarantor have been completed or are ongoing in accordance with the applicable FDA requirements; any products exported by the Company or a Guarantor have been exported in compliance with the FDC Act; and each of the Company and the Guarantors is in compliance in all material respects with the provisions of the Prescription Drug Marketing Act, to the extent applicable.

(c) Without limiting the general liability of the representations and warranties made in Section 4.10(a), the Company also represents and warrants that it and the Guarantors are in compliance in all material respects with all applicable provisions of the

Controlled Substances Act (the "CSA") and that the Company and the Guarantors are in compliance with the following specific requirements: the Company and the Guarantors 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 Company's knowledge, neither the Company nor any Guarantor 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.

IV.11. Sales Representatives, Customers and Key Employees. Other than as set forth in Section 4.11 of the Schedule of Exceptions or the Annual Report, to the knowledge of the Company, no independent sales representatives, customers or key employees or group of key employees of the Company or any Guarantor has any intention to terminate his, her or its relationship with the Company or such Subsidiary on or after the Closing or in the case of employees, leave, as of the Closing, the employ of the Company on and after the Closing. Other than as set forth in Section 4.11 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.

IV.12. Copyrights, Trademarks and Patents. (a) Section 4.12 of the Schedule of Exceptions sets forth a list of all of the Company's and any Guarantor'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 Company's knowledge and belief, fully valid and are in full force and effect.

(b) The Company or a Guarantor owns outright all of the Intellectual Property Rights listed on Section 4.12 of the Schedule of Exceptions attached hereto free and clear of all liens and encumbrances except for the Permitted Encumbrances and pays no royalty to anyone under or with respect to any of them.

(c) Neither the Company nor any Guarantor has licensed anyone to

use any of such Intellectual Property Rights and has no knowledge of the infringing use by the Company or any Guarantor of any intellectual property rights.

(d) The Company 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 Company and the Guarantors or with respect to any license under which the Company or a Guarantor is licensor or licensee; or (ii) that the Intellectual Property Rights infringe upon the rights of any third party.

IV.13. Inventory. All inventory of the Company 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 consolidated balance sheet of the Company and its Subsidiaries as of December 31, 1998. 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 Company.

IV.14. Registration Rights. Except as provided for in this Agreement or as set forth in Section 4.14 of the Schedule of Exceptions or in the Annual Report, neither the Company nor any Guarantor is under any obligation to register any of its currently outstanding securities or any of its securities which may hereafter be issued.

IV.15. No Discrimination; Labor Matters. Neither the Company nor any Guarantor in any manner or form discriminates, fosters discrimination or permits discrimination against any person based on gender or age, or belonging to any minority race or believing in any minority creed or religion. The Company is in material compliance with all applicable laws respecting employment practices, terms and conditions of employment and wages and hours and is not and has not engaged in any unfair labor practice. There is no unfair labor practice charge or complaint against the Company pending before the National Labor Relations Board or any other governmental agency arising out of the Company's activities and the Company has no knowledge of any facts or information that would give rise thereto; there is no labor strike or labor disturbance pending or threatened against the Company nor is any grievance currently being asserted.

IV.16. Environmental Matters.

(a) Each of the Company and the Guarantors 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 could not reasonably be expected to have a Material Adverse Effect on the Company or the

Guarantors), and all such permits are in full force and effect and each of the Company and the Guarantors is in compliance in all material respects with all terms and conditions of such permits.

(b) Except as set forth in Section 4.16 of the Schedule of Exceptions or the Annual Report, there is no proceeding pending or, to the best knowledge of the Company, threatened, which may result in the denial, rescission, termination, modification or suspension of any environmental or heath or safety permits necessary for the operation of the business of the Company and the Guarantors.

(c) Except as set forth in Section 4.16 of the Schedule of Exceptions or the Annual Report, during the occupancy by the Company or any Guarantor of any real property owned or leased by the Company or such Guarantor, neither the Company nor any Guarantor, and to the best knowledge of the Company, 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 laws. To the best knowledge of the Company, there are no underground storage tanks and no polychlorinated biphenyls ("PCB's"), PCB contaminated oil or asbestos on any property leased by the Company or any Guarantor.

(d) Except as set forth in Section 4.16 of the Schedule of Exceptions or the Annual Report, neither the Company nor any Guarantor 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 the Company's knowledge, each of the Company and the Guarantors has disposed of all waste in full compliance with all environmental laws.

IV.17. Taxes. Except as set forth in Section 4.17 of the Schedule of Exceptions or the Annual Report, the Company and each of the Guarantors 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 Company has no knowledge of any tax deficiency which might be assessed against the Company or any Guarantor which, if so assessed, could reasonably be expected to have a Material Adverse Effect on the Company or the Guarantors.

IV.18. Employee Benefit Plans and Similar Arrangements.

(a) Section 4.18 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 Company, the Guarantors, and any of its ERISA Affiliates are a party or by which the Company, the Guarantors, 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 Internal Revenue Code of 1986, as amended (the "Code")) as the Company, 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 the meaning of Section 414(c) of the Code) with the Company, 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 Company, 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 Company, its Subsidiaries, and each ERISA Affiliate, as applicable, have been delivered to Oracle, as agent: (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 Internal Revenue Service ("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 4.18 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 Company, 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 Company, any Subsidiary, or any ERISA Affiliate to make timely installments or other payments required under Code Section 412.

(e) Except as shown on Section 4.18 of the Schedule of Exceptions or in the Annual Report, 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 4.18 of the Schedule of Exceptions, to the best knowledge of the Company, its Subsidiaries, and ERISA Affiliates, there are no pending or threatened claims, investigations, 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 Company, its Subsidiaries, or any ERISA Affiliate may be directly or indirectly liable, through indemnification obligations or otherwise.

(g) Neither the Company, 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) Except as shown on Section 4.18 of the Schedule of Exceptions, within the last five years, neither the Company, 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 Company, 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.

4.19. Personal Property. The Company and the Guarantors have good and marketable title to each item of equipment, machinery, furniture, fixtures, vehicles, structures

and other personal property, tangible and intangible, included as an asset in the Financial Statements filed as part of the Company's Annual Report and as part of its Form 10-Q for the period ended March 31, 1999 free and clear of any security interests, options, liens, claims, charges or encumbrances whatsoever, except as set forth in Schedule 4.7 hereto and as disclosed in the Company General Security Agreement and the Guarantors General Security Agreement executed in connection herewith. The tangible personal property owned by the Company or used by the Company on the date hereof in the operation of its business is adequate for the business conducted and proposed to be conducted by the Company.

4.20. Real Property. The Company and the Guarantors do not own any fee simple interest in real property other than as set forth on Schedule 4.20 (the "Owned Property"). The Company and the Guarantors do not lease or sublease any real property other than as set forth on Schedule 4.20 (the "Leased Property"). The Company has previously delivered to Purchaser a true and complete copy of all of the lease and sublease agreements, as amended to date (the "Leases") relating to the Owned Property and the Leased Property. The Company enjoys a peaceful and undisturbed possession of the Owned Property and Leased Property. No person other than the Company has any right to use or occupy any part of the Owned Property and the Leased Property. The Leases are valid, binding and in full force and effect, all rent and other sums and charges payable thereunder are current, no notice of default or termination under any of the Leases is outstanding, no termination event or condition or uncured default on the part of the Company or, to the best of the Company's knowledge, on the part of the landlord or sublandlord, as the case may be, thereunder, exists under the Leases, and no event has occurred and no condition exists which, with the giving of notice or the lapse of time or both, would constitute such a default or termination event or condition. There are no sub-leases, licenses or other agreements granting to any person other than the Company or the Guarantors any right to possession, use, occupancy or enjoyment of the Premises demised by the Leases. All of the Premises are used in the conduct of the Company's or the Guarantors' business.

All material permits, licenses, franchises, approvals and authorizations (collectively, the "Real Property Permits") of all governmental authorities having jurisdiction over each Leased Property and from all insurance companies and fire rating and other similar boards and organizations (collectively, the "Insurance Organizations"), required have been issued to the Company and the Guarantors to enable each Leased Property to be lawfully occupied and used for all the purposes for which they are currently occupied and used and have been lawfully issued and are, as of the date hereof, in full force and effect.

Neither the Company nor the Guarantors have received any notice nor have they any knowledge of any pending, threatened or contemplated condemnation proceeding affecting any Leased Property or any part thereof.

4.21. Disclosure. The information heretofore provided and to be provided pursuant to this Agreement, including the Schedules of Exceptions and the Exhibits hereto, and each of the agreements, documents, certificates and writings previously delivered to the

Purchasers or their 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. There is no fact which could reasonably be expected to have a Material Adverse Effect on the Company or the Guarantors or the prospects of the Company or the Guarantors which has not been set forth herein.

ARTICLE V

REPRESENTATIONS AND WARRANTIES OF THE PURCHASERS

Each of the Purchasers severally represents and warrants to the Company that it is acquiring the Securities for investment for its own account and is not acquiring any of the Securities with the view to, or for resale in connection with, any distribution thereof. Each Purchaser understands that none of the Securities have been registered under the Securities Act. If the Purchaser should in the future decide to dispose of any Securities it is understood that the Purchaser may do so only in compliance with the Securities Act. Each Purchaser will be required to complete and execute the form of Subscription Agreement attached as Exhibit J hereto. Purchaser acknowledges that the Company will rely upon the representations made by such Purchaser in the Subscription Agreement in connection with the issuance of the Securities to be sold hereunder.

ARTICLE VI

CONDITIONS TO CLOSING OF THE PURCHASERS

The obligation of each Purchaser to purchase the Securities at the Closing is subject to the fulfillment to such Purchaser's satisfaction on or prior to the Closing Date of each of the following conditions, any of which may be waived by such Purchaser:

VI.1. Representations and Warranties Correct. The representations and warranties in Article 4 hereof shall be true and correct when made, and shall be true and correct on the Closing Date with the same force and effect as if they had been made on and as of the Closing Date.

VI.2. Performance. All covenants, agreements and conditions contained in this Agreement to be performed or complied with by the Company on or prior to the Closing Date shall have been performed or complied with by the Company in all material respects.

VI.3. Compliance Certificate. The Company shall have delivered to the Purchaser a certificate of the Company's President, dated the Closing Date, certifying to the fulfillment of the conditions specified in Sections 6.1 and 6.2 of this Agreement and other

matters as the Purchaser shall reasonably request.

VI.4. No Impediments. Neither the Company nor any Purchaser shall be subject to any order, decree or injunction of a court or administrative agency of competent jurisdiction which would impose any material limitation on the ability of such Purchaser to exercise full rights of ownership of the Securities.

VI.5. Waivers/Elections of Rights of First Refusal. The Company shall have obtained from each person other than a Purchaser who has any current effective right of first refusal with respect to the Securities, a written waiver or election of such right in form and substance reasonably satisfactory to the Purchasers.

VI.6. Other Agreements and Documents. The Company shall have issued to such Purchaser all of the Securities (including the Debenture, the $1.404 Warrants and the $2.285 Warrants) and the Company or each of the Guarantors shall have executed and delivered the following agreements and documents:

(a) The Company Security Agreement in the form of Exhibit F attached hereto;

(b) The Guaranties in the form of Exhibit G attached hereto;

(c) The Guarantors Security Agreement in the form of Exhibit H attached hereto;

(d) Financing Statements on Form UCC-1 with respect to all personal property and assets of the Company and each Guarantor;

(e) A certified copy of the Certificate of Incorporation of the Company and each Guarantor and all amendments thereto;

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

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

(h) The Mortgage; and

(i) Intercreditor Agreement in the form of Exhibit I attached hereto.

VI.7. Consents. The Company shall have obtained all necessary consents or

waivers, if any, from all parties to any other material agreements to which the Company 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 the Company may be conducted by the Company after the Closing without adversely affecting the Company.

VI.8. Legal Investment. At the time of the Closing, the purchase of the Securities to be purchased by each Purchaser hereunder shall be legally permitted by all laws and regulations to which the Purchasers and the Company are subject.

VI.9. Proceedings and Other Documents. All corporate and other proceedings in connection with the transactions contemplated by this Agreement shall have been taken and the Purchasers shall have received such other documents, in form and substance reasonably satisfactory to the Purchasers and their counsel, as to such other matters incident to the transaction contemplated hereby as the Purchasers may reasonably request.

VI.10. Opinion of Counsel. The Purchasers shall have received the opinion of St. John & Wayne, L.L.C., counsel to the Company, dated the Closing Date, substantially in the form of Exhibit J attached hereto.

VI.11. Nomination of Director. One designee of the Purchasers shall have been nominated for election as a director of the Company for consideration at the Company's 1999 Annual Meeting of Shareholders.

ARTICLE VII

CONDITIONS TO CLOSING OF THE COMPANY

The Company's obligation to sell the Securities at the Closing is subject to the fulfillment to its satisfaction on or prior to the Closing Date of each of the following conditions:

VII.1. Representations. The representations made by each Purchaser pursuant to Article 5 hereof and in the Subscription Agreement shall be true and correct when made and shall be true and correct on the Closing Date.

VII.2. Legal Investment. At the time of the Closing, the purchase of the Securities shall be legally permitted by all laws and regulations to which the Purchasers and the Company are subject.

VII.3. Payment of Purchase Price. The Company shall have received payment in full of the purchase price for the Securities.

ARTICLE VIII

PREPAYMENT

VIII.1. No Optional Prepayments. The Company may not at any time, without the prior written consent of the holders of all outstanding Debentures, prepay any Debenture, in whole or in part.

ARTICLE IX

AFFIRMATIVE COVENANTS

The Company hereby covenants and agrees, so long as any Securities remain outstanding, as follows:

IX.1. Maintenance of Corporate Existence, Properties and Leases; Taxes; Insurance.

(a) The Company shall and shall cause each of 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 Company 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 Company 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 Company shall and shall cause each of the Guarantors to, except as otherwise described in the Annual Report, 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 Company 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 Company or the Guarantors; provided, however, that any such tax, lien, 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 Company or the Guarantors 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 holders of the Securities, and provided, further, that the Company or the Guarantors will pay or cause to be paid any such tax, lien, assessment, charge or levy forthwith upon the commencement of proceedings to foreclose any lien which may have attached as security therefor. The Company shall and shall cause the Guarantors to pay or cause to be paid all other indebtedness incident to the operations

of the Company or the Guarantors.

(d) The Company shall and shall cause each of the Guarantors to, keep its 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 line of business of the Company or the Guarantors, in amounts sufficient to prevent the Company or the Guarantors from becoming a co-insurer of the property insured; and the Company 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 Company or the Guarantors is a party or by which it is bound.

IX.2. Basic Financial Information. The Company shall furnish the following reports to each Purchaser (or any transferee of any Securities), so long as the Purchaser is a holder of any Securities:

(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 Company's Board of Directors, if earlier), unaudited consolidated statements of income and retained earnings and cash flows of the Company 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 Company 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 generally accepted accounting principles, 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 Company 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 generally accepted accounting principles, consistently applied (except as approved by the accounting firm examining such statements and disclosed by the Company), and will be accompanied by:

(i) an unqualified report of the Company's independent certified public accounting firm;

(ii) a report from such accounting firm addressed to the Purchasers, stating that in making the audit necessary to express their opinion on the financial statements, nothing has come to their attention which would lead them to believe that the Company is not in

compliance with the financial covenants contained in, or that an Event of Default has occurred with respect to, this Agreement or the Debentures (an "Event of Non-Compliance") or, if such accountants have reason to believe that any Event of Non-Compliance 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 Company stating that the Company is in compliance with the terms of this Agreement and any other material contract or commitment to which the Company or any of its Subsidiaries is a party or by which any of them is bound, or if the Company or any of its Subsidiaries is not in compliance, specifying the nature and period of noncompliance, and what actions the Company 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 Company shall be signed by both the Chief Executive Officer and the Chief Financial Officer of the Company 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 Company and its Subsidiaries, given to the Company 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 Company 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 Company) behind the projections contained in such financial statements, and which budgets shall have been approved by the Board of Directors of the Company 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 Company 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 Company 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 Company are then listed or proposed to be listed, copies of all press releases and other statements made generally available by the Company to the public concerning material developments in the business of the Company and its Subsidiaries and copies of material

communications sent to or received from stockholders, directors or committees of the Board of Directors of the Company or any of its Subsidiaries and copies of all material communications sent to and received from any lender to the Company; and

(g) with reasonable promptness such other information and financial data concerning the Company as any person entitled to receive materials under this Section 9.2 may reasonably request.

IX.3. Notice of Adverse Change. The Company shall promptly give notice to all holders of any Securities (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 Default;

(b) the institution or threatening of institution of an action, suit or proceeding against the Company 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 Company and its Subsidiaries, taken as a whole whether or not arising in the ordinary course of business; or

(c) any information relating to the Company or any Subsidiary which could reasonably be expected to materially and adversely affect the assets, property, business or condition (financial or otherwise) of the Company or its ability to perform the terms of this Agreement. Any notice given under this Section 9 shall specify the nature and period of existence of the condition, event, information, development or circumstance, the anticipated effect thereof and what actions the Company has taken and/or proposes to take with respect thereto.

IX.4. Compliance With Agreements; Compliance With Laws. The Company shall comply and cause its Subsidiaries to comply, with the terms and conditions of all material agreements, commitments or instruments to which the Company or any of its Subsidiaries is a party or by which it or they may be bound. The Company shall and shall cause each of its Subsidiaries to duly 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, the requirements of the FDA Act, the Prescription Drug Marketing Act, the CSA, the Employee Retirement Income Security Act of 1978, the Environmental Protection Act, the Occupational Safety and Health Act, the Foreign Corrupt Practices Act and the rules and regulations of each of the agencies administering such acts.

IX.5. Protection of Licenses, etc. The Company 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 Company 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 Company.

IX.6. Accounts and Records; Inspections.

(a) The Company 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 Company and its Subsidiaries in accordance with generally accepted accounting principles applied on a consistent basis.

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

(c) Nothing contained in this Section 9.6 shall be construed to limit any rights which a holder of any Securities (a "Holder") may have with respect to the books and records of the Company and its Subsidiaries, to inspect its properties or to discuss its affairs, finances and accounts.

IX.7. Board Members and Meetings.

The Company agrees to hold meetings of its Board of Directors at least four (4) times a year, at no more than three-month intervals. So long as the Purchasers own any Debentures, the Purchasers (by action of the holders of a majority of the outstanding principal amount of the Debentures) shall have the right to designate for nomination one person to be a member of the Company's Board of Directors and the Company shall cause such designee to be nominated on the Closing Date, subject to the approval of the Company's shareholders for (i) the election of such designee and (ii) an amendment to the Company's certification of incorporation to increase the size of the Board of Directors. So long as the Purchasers own any Debentures, at each annual meeting of Stockholders held thereafter, the Purchasers (by action of the holders of a majority of the outstanding principal amount of the Debentures) shall have the right to nominate one designee to be a member of the Board of Directors.

IX.8. Maintenance of Office. The Company will maintain its principal office at

the address of the Company set forth in Section 16.5 of this Agreement where notices, presentments and demands in respect of this Agreement and any of the Securities may be made upon the Company, until such time as the Company shall notify the holders of the Securities in writing, at least thirty (30) days prior thereto, of any change of location of such office.

IX.9. Use of Proceeds. The Company shall use all the proceeds received from the sale of the Securities pursuant to this Agreement for the purposes set forth in Section 9.9 of the Schedule of Exceptions.

IX.10. Payment of Debentures. The Company shall pay the principal of and interest on the Debentures in the time, the manner and the form provided therein.

IX.11. Reporting Requirements. The Company shall comply with its reporting and filing obligations pursuant to Section 13 or 15(d) of the Exchange Act. The Company 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 each holder of Securities promptly upon filing with the Commission.

IX.12. Amendments to the Company's Certificate of Incorporation.

(A) The Company will present to its shareholders for consideration at the 1999 Annual Meeting of Shareholders (i) a proposal to amend the Company's Certificate of Incorporation to increase the number of authorized shares of the Company's common stock available for issuance from 40,000,000 to 75,000,000 shares in order to provide for a sufficient number of authorized shares to be available and reserved for issuance upon conversion of the Debentures and exercise of the Warrants, (ii) a proposal to amend the Company's Certificate of Incorporation to provide that holders of Debentures shall have the right to vote as part of a single class with all holders of Common Stock of the Company on all matters to be voted on by such stockholders with such Holder having such number of votes as shall equal the number of votes they would have had such Holders converted the entire outstanding principal amount of the Debentures into Shares immediately prior to the record date relating to such vote, (iii) a proposal to obtain shareholder approval to permit the issuance of the Company's Common Stock in an amount exceeding twenty percent (20%) of the Company's outstanding Common Stock on the date of this Agreement pursuant to the conversion of the Debentures and exercise of the Warrants, (iv) a proposal to amend the Company's Certificate of Incorporation to increase the size of the Board of Directors from a maximum of eight (8) to a maximum of eleven (11) directors, and (v) the nomination for director of a designee of the Purchasers (as designated by the holders of a majority of the outstanding principal amount of the Debentures). Upon receipt of approval from the Company's shareholders to increase the Company's authorized shares from 40,000,000 to 75,000,000 shares, the Company will file an amendment to the Certificate of Incorporation to reflect such increase in the Company's authorized shares to 75,000,000 shares of Common Stock and at all times cause there to be reserved for issuance a sufficient number of Shares upon conversion of the Debentures and exercise of the Warrants.

(B) Upon execution of this Purchase Agreement, the Company shall use its best efforts to promptly file with the Federal Trade Commission and the Department of Justice, but in no event later than sixty (60) days from the date of this Purchase Agreement, all required Pre-Merger Notifications and Reports ("Notifications") pursuant to the Hart-Scott-Rodino Anti-Trust Improvements Act of 1976, as amended ("HSR Act") in conjunction with a corresponding filing by Galen Partners III, L.P. and Galen Partners International III, L.P. (collectively, "Galen"), in order to permit the Company to file the amendment to its Certificate of Incorporation approved at the Company's Annual Shareholder's Meeting held on June 30, 1998 providing the holders of the Company's 5% Convertible Senior Secured Debentures due March 15, 2003 ("March 1998 Debentures") with the right to vote as part of a single class with all holders of the Company's Common Stock on all matters to be voted on by such stockholders on a "as converted" basis (the "Charter Amendment"). Promptly upon the satisfaction of the waiting period required under the HSR Act, the Company shall file with the Secretary of State of the State of New York the Charter Amendment and convene a special meeting of the Company shareholders (the "Special Meeting") to reconsider the proposals described in Section 9.12(A)(i), (ii) and (iii) in the event such proposals were not approved at the Company's Annual Shareholders Meeting. By execution of this Agreement by counterpart solely as to the provisions of this Section 9.12(B), Galen agrees to file its required Notifications under the HSR Act and to exercise its voting rights provided under the Charter Amendment at the Special Meeting and cast all such votes in favor of the proposals described above at the Special Meeting.

IX.13. Listing of Common Stock. As promptly as practicable following receipt of shareholder approval of the amendment to the Company's Certificate of Incorporation contemplated in Section 9.12 hereof, the Company shall file the appropriate applications for listing with the AMEX the shares underlying the Debentures and Warrants. The Company shall use its best efforts and work diligently to accomplish such listings as promptly as practicable after the 1999 Annual Meeting of Shareholders.

IX.14. HSR Act Filing. The Purchasers acknowledge and agree that until the filing, if required, of all Pre-Merger Notifications and reports ("Notifications") pursuant to the Hart-Scott-Rodino Antitrust Improvements Act of 1976, as amended (the "HSR Act"), with respect to the issuance of the Securities and the expiration or termination of all applicable waiting periods thereunder, a Certificate of Amendment to the Certificate of Incorporation of the Company providing for voting rights for the Holders will not be filed. The Company agrees to file all Notifications, if any, required to be filed by it under the HSR within sixty (60) days after the date hereof.

IX.15. Further Assurances. From time to time the Company shall execute and deliver to the Purchasers and the Purchasers shall execute and deliver to the Company 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 Agreement and any of the Securities.

ARTICLE X

NEGATIVE COVENANTS

The Company hereby covenants and agrees, so long as any Purchaser owns any Debentures, it will not (and not allow any of the Guarantors to), directly or indirectly, without the prior written consent of the holders of at least a majority in aggregate principal amount of the Debentures then outstanding, as follows:

X.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 Company, 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 Company or warrants or rights to acquire such capital stock.

X.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 Debentures, the Company 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 Holders but will suffer and permit the execution of every such power as though no such law had been enacted.

X.3. Reclassification. Effect any reclassification, combination or reverse stock split of the common stock of the Company.

X.4. Liens. Except as otherwise provided in this 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 generally accepted accounting principles 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 Company;

(c) liens securing indebtedness of the Company or any Subsidiaries which (i) is permitted under Section 10.5(h) or (ii) is in an aggregate principal amount not exceeding

$500,000 and which liens are subordinate to liens on the same assets held by the Holders;

(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 generally accepted accounting principles 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 Company 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 Company and its Subsidiaries;

(l) the liens listed in Section 10.4 of the Schedule of Exceptions ("Permitted Liens"); and

(m) the replacement, extension or renewal of any lien permitted by this Section 10.4 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.

X.5. 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 10.4 (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 Company 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 10.5 of the Schedule of Exceptions;

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

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

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

(h) indebtedness relating to a working capital line of credit in an amount not to exceed $10,000,000;

(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 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 Company (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 Company (or Subsidiary) for which the Company (or Subsidiary) is obligated, contingently or otherwise, to purchase or otherwise acquire, or for the payment or purchase of which the Company (or Subsidiary) has agreed, contingently or otherwise, to advance or supply funds, or with respect to which the Company (or Subsidiary) is contingently liable, including, without limitation, indebtedness for borrowed money and indebtedness guaranteed or supported indirectly by the Company (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 depositary, agency or trustee in trust for the payment thereof, or (y) as to which the Company (or Subsidiary) is in good faith contesting, provided that an adequate reserve therefor has been set up on the books of the Company (or Subsidiary).

X.6. Merger, Consolidation, etc. Merge or consolidate with any person pursuant to a transaction in which the outstanding voting stock of the Company is converted into or exchanged for cash, securities or other property, other than any such transaction where the outstanding voting stock of the Company is converted into or exchanged for voting stock of the surviving or transferee corporation and the beneficial owners of the voting stock of the Company immediately prior to such transaction own, directly or indirectly, not less than 66_% of the voting stock of the surviving or transferee corporation immediately after such transaction; or sell, transfer, lease or otherwise dispose of all or substantially all of its consolidated assets (as shown on the most recent financial statements of the Company or the Subsidiary, as the case may be) in any single transaction or series of related transactions; or liquidate, dissolve, recapitalize or reorganize in any form of transaction.

X.7. 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.

ARTICLE XI

REGISTRATION RIGHTS

XI.1. Restrictive Legend. Each certificate representing (i) any Debenture, (ii) the Warrants or (iii) any Shares or other securities issued in respect of the Debentures, Warrants or

Shares, upon any stock split, stock dividend, recapitalization, merger, consolidation or similar event or upon the exercise of the Warrants or conversion of the Debentures, shall be stamped or otherwise imprinted with a legend in the following form (in addition to any legend required under applicable state securities laws):

"THIS [NAME OF SECURITY] [AND THE COMMON STOCK ISSUABLE UPON [CONVERSION] [EXERCISE] HEREOF] HAVE NOT BEEN REGISTERED UNDER THE SECURITIES ACT OF 1933, AS AMENDED, NOR ANY STATE SECURITIES LAW AND MAY NOT BE PLEDGED, SOLD, ASSIGNED, HYPOTHECATED OR OTHERWISE TRANSFERRED UNTIL (1) A REGISTRATION STATEMENT WITH RESPECT THERETO IS EFFECTIVE UNDER THE ACT AND ANY APPLICABLE STATE SECURITIES LAW OR (2) THE COMPANY RECEIVES AN OPINION OF COUNSEL TO THE COMPANY OR OTHER COUNSEL TO THE HOLDER OF SUCH [NAME OF SECURITY] REASONABLY SATISFACTORY TO THE COMPANY THAT SUCH [NAME OF SECURITY] [AND/OR COMMON STOCK] MAY BE PLEDGED, SOLD, ASSIGNED, HYPOTHECATED OR TRANSFERRED WITHOUT AN EFFECTIVE REGISTRATION STATEMENT UNDER THE ACT OR APPLICABLE STATE SECURITIES LAWS.

XI.2. Certain Definitions. As used in this Article 11, the following terms shall have the following respective meanings:

"Holders" shall mean the Purchasers or any person to whom a Purchaser or transferee of a Purchaser has assigned any Debenture, Warrants or Shares.

"Initiating Holders" shall mean any persons who in the aggregate are Holders of at least a majority of the Shares.

"Registrable Securities" shall mean any Shares issued upon exercise of the Warrants, conversion of any Debenture or in respect of the Shares issued upon exercise of the Warrants or conversion of any Debenture upon any stock split, stock dividend, recapitalization or similar event. "Requesting Stockholders" shall mean holders of securities of the Company entitled to have securities included in any registration pursuant to Section 11.3 and who shall request such inclusion.

The terms "register," "registered" and "registration" shall refer to a registration effected by preparing and filing a registration statement in compliance with the Securities Act and applicable rules and regulations thereunder, and the declaration or ordering of the effectiveness of such registration statement.

"Registration Expenses" shall mean all expenses incurred by the Company in

compliance with Sections 11.3 and 11.4 hereof, including, without limitation, all registration and filing fees, printing expenses, fees and disbursements of counsel for the Company and blue sky fees and expenses, reasonable fees and disbursements for one counsel for the Initiating Holders, and the expense of any special audits incident to or required by any such registration, exclusive of Selling Expenses.

"Restricted Securities" shall mean the securities of the Company required to bear or bearing the legend set forth in Section 11.1 hereof.

"Selling Expenses" shall mean all underwriting discounts and selling commissions applicable to the sale of Registrable Securities and, except as otherwise provided in "Registration Expenses", all fees and disbursements of counsel for any Holder.

XI.3. Requested Registration.

(a) Requests for Registration. The Initiating Holders may request registration under the Securities Act of all or part of their Registrable Securities. Within ten (10) days after receipt of any such request, the Company will give written notice of such requested registration to all other Holders of Registrable Securities and any other stockholder having registration rights which entitle it to participate in such registration. The Company will include in such registration all Registrable Securities with respect to which it has received written requests for inclusion therein within fifteen (15) days after receipt of the Company's notice. The Company shall cause its management to cooperate fully and to use its best efforts to support the registration of the Registrable Securities and the sale of the Registrable Securities pursuant to such registration as promptly as is practicable. Such cooperation shall include, but not be limited to, management's attendance and reasonable presentations in respect of the Company at road shows with respect to the offering of Registrable Securities. The registration requested under this Section 11.3(a) is referred to herein as a "Demand Registration."

(b) Number of Registrations. The Holders of Registrable Securities will be entitled to request one (1) Demand Registration for which the Company will pay all Registration Expenses. A registration will not count as a Demand Registration until it has become effective; provided, however, that whether or not it becomes effective the Company will pay all Registration Expenses in connection with any registration so initiated.

(c) Priority on Demand Registrations. If a Demand Registration is an underwritten offering, and the managing underwriters advise the Company in writing that in their opinion the number of Registrable Securities requested to be included exceeds the number which can be sold in such offering, the Company will include in such registration such number of Shares, which in the opinion of such underwriters, may be sold, allocated among the Holders electing to participate pro rata in accordance with the amounts of securities requested to be so included by the respective Holders. The Company will not include in any Demand Registration any securities which are not Registrable Securities without the written consent of the Holders of

a majority of the Registrable Securities requesting such registration. Any persons other than Holders of Registrable Securities who participate in a Demand Registration which is not at the Company's expense must pay their share of the Registration Expenses. A registration shall not count as a Demand Registration if some or all of the Shares which any Holder desires to include therein are not included due to the determination of the managing underwriters referred to in the first sentence of this Section 11.3(c).

(d) Restrictions on Demand Registrations. The Company will not be obligated to effect any Demand Registration within six (6) months after the effective date of a previous registration in which the Holders of Registrable Securities were given piggyback rights pursuant to Section 11.4 other than a registration of Registrable Securities intended to be offered on a continuous or delayed basis under Rule 415 or any successor rule under the Securities Act (a "Shelf Registration").

XI.4. Piggyback Registrations.

(a Right to Piggyback. Whenever the Company proposes to register any of its securities under the Securities Act (other than pursuant to a Demand Registration or pursuant to a registration on Forms S-4 or S-8 or any successors to such forms) and the registration form to be used may be used for the registration and contemplated disposition of Registrable Securities (a "Piggyback Registration"), the Company will give prompt written notice to all Holders of Registrable Securities of its intention to effect such a registration. The Company will include in such registration all Registrable Securities with respect to which the Company has received written requests for inclusion therein within thirty (30) days after the receipt of the Company's notice.

(b Piggyback Expenses. The Registration Expenses of the Holders of Registrable Securities will be paid by the Company.

(c Priority on Primary Registrations. If a Piggyback Registration is an underwritten primary registration on behalf of the Company, and the managing underwriters advise the Company in writing that in their opinion the number of securities requested to be included in such registration exceeds the number which can be sold in such offering, the Company will include in such registration (i) first, the securities the Company proposes to sell, (ii) second, the Registrable Securities and securities of the Company with respect to which similar registration rights have heretofore been granted and requested to be included in such registration, pro rata in accordance with the amounts of Registrable Securities and such securities requested to be so included by the respective Holders and holders of such securities of the Company; and (iii) third, any other securities requested to be included in such registration.

(d Priority on Secondary Registrations. If a Piggyback Registration is an underwritten secondary registration on behalf of holders of the Company's securities, and the managing underwriters advise the Company in writing that in their opinion the number of

securities requested to be included in such registration exceeds the number which can be sold in such offering, the Company will include in such registration (i) first, the securities requested to be included therein by the holders requesting such registration, (ii) second, the Registrable Securities and securities of the Company with respect to which similar registration rights have heretofore been granted and requested to be included in such registration, pro rata in accordance with the amounts of Registrable Securities and such securities requested to be so included by the respective Holders and holders of such securities of the Company, and (iii) third, other securities requested to be included in such registration.

(e Other Restrictions. The Company hereby agrees that if it has previously filed a registration statement with respect to Registrable Securities pursuant to Section 11.3 or pursuant to this Section 11.4, and if such previous registration has not been withdrawn or abandoned, the Company will not file or cause to be effected any other registration of any of its equity securities or securities convertible or exchangeable into or exercisable for its equity securities under the Securities Act (except on Form S-8 or any other similar form for employee benefit plans), whether on its own behalf or at the request of any holder or holders of such securities, until a period of at least six (6) months has elapsed from the effective date of such previous registration or, if sooner, until all Registrable Securities included in such previous registration have been sold.

XI.5. Holdback Agreements.

(a Each Holder of Registrable Securities which is a party to this Agreement agrees not to effect any public sale or distribution of equity securities of the Company, or any securities convertible into or exchangeable or exercisable for such securities, during the seven (7) days prior to and the 90-day period beginning on the effective date of any underwritten Demand Registration or any underwritten Piggyback Registration (except as part of such underwritten registration) or, if sooner, until all Registrable Securities included within such registration have been sold.

(b The Company agrees (i) not to effect any public sale or distribution of its equity securities, or any securities convertible into or exchangeable or exercisable for such securities, during the seven (7) days prior to and the 90-day period beginning on the effective date of any underwritten Demand Registration or any underwritten Piggyback Registration (except as part of such underwritten registration or pursuant to registrations on Form S-8 or any other similar form for employee benefit plans) or, if sooner, until all Registrable Securities included within such registration have been sold, and (ii) to use its reasonable best efforts to cause each holder of its equity securities, or any securities convertible into or exchangeable or exercisable for such securities, purchased from the Company at any time after the date of this Agreement (other than in a registered public offering) to agree not to effect any public sale or distribution of any such securities during such period (except as part of such underwritten registration, if otherwise permitted) or, if sooner, until all Registrable Securities included within such registration have been sold.

XI.6. Registration Procedures. Whenever the Holders of Registrable Securities have requested that any Registrable Securities be registered pursuant to this Article 11, the Company will use its reasonable best efforts to effect the registration and the sale of such Registrable Securities in accordance with the intended method of disposition thereof, and pursuant thereto the Company will as expeditiously as possible:

(a prepare and file with the Commission a registration statement with respect to such Registrable Securities, which registration statement will state that the Holders of Registrable Securities covered thereby may sell such Registrable Securities either under such registration statement or, at any Holder's proper request, pursuant to Rule 144 (or any similar rule then in effect), and use its best efforts to cause such registration statement to become effective (provided that before filing a registration statement or prospectus or any amendments or supplements thereto, the Company will furnish to the counsel selected by the Holders of a majority of the Registrable Securities covered by such registration statement copies of all such documents proposed to be filed, which documents will be subject to the review of such counsel);

(b prepare and file with the Commission such amendments and supplements to such registration statement and the prospectus used in connection therewith as may be necessary to keep such registration statement effective for the period set forth in Section 11.6(i) hereof and comply with the provisions of the Securities Act with respect to the disposition of all securities covered by such registration statement during such period in accordance with the intended methods of disposition by the sellers thereof set forth in such registration statement;

(c furnish to each seller of Registrable Securities such number of copies of such registration statement, each amendment and supplement thereto, the prospectus included in such registration statement (including each preliminary prospectus) and such other documents as such seller may reasonably request in order to facilitate the disposition of the Registrable Securities owned by such seller;

(d use its best efforts to register or qualify such Registrable Securities under such other securities or blue sky laws of such jurisdictions as any seller reasonably requests and do any and all other acts and things which may be reasonably necessary or advisable to enable such seller to consummate the disposition in such jurisdictions of the Registrable Securities owned by such seller (provided that the Company will not be required to (i) qualify generally to do business in any jurisdiction where it would not otherwise be required to qualify but for this subsection, (ii) subject itself to taxation in any such jurisdiction, or (iii) consent to general service of process in any such jurisdiction);

(e notify each seller of such Registrable Securities, at any time when a prospectus relating thereto is required to be delivered under the Securities Act, of the happening of any event as a result of which the prospectus included in such registration statement contains an untrue statement of a material fact or omits to state any fact necessary to make the statements therein not misleading, and, at the request of any such seller, the Company will promptly prepare

a supplement or amendment to such prospectus so that, as thereafter delivered to the purchasers of such Registrable Securities, such prospectus will not contain an untrue statement of a material fact or omit to state any fact necessary to make the statements therein not misleading;

(f cause all such Registrable Securities to be listed on each securities exchange on which similar securities issued by the Company are then listed;

(g provide a transfer agent and registrar for all such Registrable Securities not later than the effective date of such registration statement;

(h make available for inspection by any seller of Registrable Securities, any underwriter participating in any disposition pursuant to such registration statement, and any attorney, accountant or other agent retained by any such seller or underwriter, all financial and other records, pertinent corporate documents and properties of the Company, and cause the Company's officers, directors and employees to supply all information reasonably requested by any such seller, underwriter, attorney, accountant or agent in connection with such registration statement; and

(i cause the Registrable Securities to be registered on such appropriate registration form or forms of the Commission as shall permit a delayed or continuous offering of the Registrable Securities pursuant to Rule 415 under the Securities Act and permit the disposition of the Registrable Securities in accordance with the method or methods of disposition requested by the Initiating Holders and keep such registration statement effective until the Holders have completed the sale and distribution of the Registrable Securities.

XI.7. Expenses of Registration. All Registration Expenses incurred in connection with a registration, qualification or compliance pursuant to this Article 11 shall be borne by the Company, and all Selling Expenses shall be borne by the Holders and the Requesting Stockholders of the securities so registered pro rata on the basis of the number of their shares so registered; provided, however, that the Company shall not be required to pay any Registration Expenses if, as a result of the withdrawal of a request for registration by Initiating Holders, the registration statement does not become effective, in which case the Holders and Requesting Stockholders requesting registration shall bear such Registration Expenses pro rata on the basis of the number of their shares so included in the registration request, and, further, that such registration shall not be counted as a Demand Registration pursuant to Section 11.3.

XI.8. Indemnification.

(a The Company will indemnify each Holder, each Holder's officers, directors, employees, agents and partners, and each person controlling such Holder, with respect to which registration, qualification or compliance of such Holder's securities has been effected pursuant to this Article 11, and each underwriter, if any, and each person who controls any underwriter, against all claims, losses, damages and liabilities (or actions in respect thereof)

arising out of or based on any untrue statement (or alleged untrue statement) of a material fact contained in any registration statement, prospectus, offering circular or other document (including any related registration statement notification or the like) incident to any such registration, qualification or compliance, or based on any omission (or alleged omission) to state therein a material fact required to be stated therein or necessary to make the statements therein not misleading, or any violation by the Company of the Securities Act or any rule or regulation thereunder applicable to the Company and relating to action or inaction required of the Company in connection with any such registration, qualification or compliance, and will reimburse each such Holder, each Holder's officers, directors, employees, agents and partners, and each person controlling such Holder, each such underwriter and each person who controls any such underwriter, for any legal and any other expenses reasonably incurred in connection with investigating or defending any such claim, loss, damage, liability or action, provided, that the Company will not be liable in any such case to the extent that any such claim, loss, damage, liability or action arises out of or is based on any untrue statement or omission of material fact based upon written information furnished to the Company by such Holder or underwriter and stated to be specifically for use therein.

(b Each Holder and Requesting Stockholder will, if Registrable Securities held by it are included in the securities as to which such registration, qualification or compliance is being effected, indemnify the Company, each of the Company's directors and officers and each underwriter, if any, of the Company's securities covered by such registration statement, each person who controls the Company or such underwriter within the meaning of the Securities Act and the rules and regulations thereunder, each other Holder and Requesting Stockholder and each of their officers, directors, employees, agents and partners, and each person controlling such Holder or Requesting Stockholder, against all claims, losses, damages and liabilities (or actions in respect thereof) arising out of or based on any untrue statement (or alleged untrue statement) of a material fact contained in any such registration statement, prospectus, offering circular or other document incident to any such registration, qualification or compliance, or based on any omission (or alleged omission) to state therein a material fact required to be stated therein or necessary to make the statements therein not misleading, and will reimburse the Company, its officers and directors, each underwriter, each person controlling the Company or such underwriter, each other Holder and Requesting Stockholders, their officers, directors, employees, agents, partners and control persons for any legal or any other expenses reasonably incurred in connection with investigating or defending any such claim, loss, damage, liability or action, in each case to the extent, but only to the extent, that such untrue statement (or alleged untrue statement) or omission (or alleged omission) is made in such registration statement, prospectus, offering circular or other document in reliance upon and in conformity with written information furnished to the Company by such Holder or Requesting Stockholder and stated to be specifically for use therein; provided, however, that the obligations of each Holder and Requesting Stockholders hereunder shall be limited to an amount equal to the proceeds (after deduction of underwriting discounts, if any) to each such Holder or Requesting Stockholder of securities sold as contemplated herein.

(c Each party entitled to indemnification under this Section 11.8 (the "Indemnified Party") shall give notice to the party required to provide indemnification (the "Indemnifying Party") promptly after such Indemnified Party has actual knowledge of any claim as to which indemnity may be sought, and shall permit the Indemnifying Party to assume the defense of any such claim or any litigation resulting therefrom, provided, that counsel for the Indemnifying Party, who shall conduct the defense of such claim or any litigation resulting therefrom, shall be approved by the Indemnified Party (whose approval shall not be unreasonably withheld) and the Indemnified Party may participate in such defense at such party's expense, and provided, further, that the failure of any Indemnified Party to give notice as provided herein shall not relieve the Indemnifying Party of its obligations under this Article 11 unless such failure has had a material adverse effect on such claim. The parties to this Agreement reserve any rights to claim under this Agreement for damages actually incurred by reason of any failure of the Indemnified Party to give prompt notice of a claim. To the extent counsel for the Indemnifying Party shall in such counsel's reasonable judgment, have a conflict in representing an Indemnified Party in conjunction with the Indemnifying Party or other Indemnified Parties, such Indemnified Party shall be entitled to separate counsel at the expense of the Indemnifying Party subject to the approval of such counsel by the Indemnified Party (whose approval shall not be unreasonably withheld). No Indemnifying Party, in the defense of any such claim or litigation, shall, except with the consent of each Indemnified Party, consent to entry of any judgment or enter into any settlement which does not include as an unconditional term thereof the giving by the claimant or plaintiff to such Indemnified Party of a release from all liability in respect of such claim or litigation. Each Indemnified Party shall furnish such information regarding itself or the claim in question as an Indemnifying Party may reasonably request in writing and as shall be reasonably required in connection with the defense of such claim and any litigation resulting therefrom.

XI.9. Information by Holders. Each Holder of Registrable Securities, and each Requesting Stockholder holding securities included in any registration, shall furnish to the Company such information regarding such Holder or Requesting Stockholder and the distribution proposed by such Holder or Requesting Stockholder as the Company may reasonably request in writing and as shall be reasonably required in connection with any registration, qualification or compliance referred to in this Article 11.

XI.10. Limitations on Registration of Issues of Securities. From and after the date of this Agreement, the Company shall not enter into any agreement with any holder or prospective holder of any securities of the Company giving such holder or prospective holder the right to require the Company to register any securities of the Company more favorable than the rights granted under this Article 11.

XI.11. Rule 144 Reporting. With a view to making available the benefits of certain rules and regulations of the Commission which may permit the sale of the Restricted Securities to the public without registration, the Company agrees to:

(a make and keep public information available as those terms are understood and defined and interpreted in and under Rule 144 under the Securities Act, at all times from and

after the date hereof;

(b file with the Commission in a timely manner all reports and other documents required of the Company under the Securities Act and the Securities Exchange Act at any time after it has become subject to such reporting requirements; and

(c so long as the Purchaser owns any Restricted Securities, furnish to the Purchaser forthwith upon request a written statement by the Company as to its compliance with the reporting requirements of Rule 144 (at any time from and after ninety (90) days following the effective date of the first registration statement filed by the Company for an offering of its securities to anyone other than its employees), and of the Securities Act and the Exchange Act (at any time after it has become subject to such reporting requirements), a copy of the most recent annual or quarterly report of the Company, and such other reports and documents so filed as the Purchaser may reasonably request in availing itself of any rule or regulation of the Commission allowing the Purchaser to sell any such securities without registration.

XI.12. Participation in Underwritten Registrations. No person may participate in any underwritten registration hereunder unless such person (i) agrees to sell such person's securities on the basis provided in any underwriting arrangements approved by the persons entitled hereunder to approve such arrangements and (ii) completes and executes all reasonable questionnaires, powers of attorney, indemnities, underwriting agreements and other documents required under the terms of such underwriting arrangements.

XI.13. Selection of Underwriters. If any Demand Registration is an underwritten offering, the Holders of a majority of the Registrable Securities included in such registration have the right to select the investment banker(s) and manager(s) to administer the offering, subject to the approval of the Company (which approval will not be unreasonably withheld). If any registration other than a Demand Registration is an underwritten offering, the Company will have the right to select the investment banker(s) and manager(s) to administer the offering, subject to the approval of the Holders of a majority of the Registrable Securities included in such registration (which approval will not be unreasonably withheld).

XI.14. Termination of Registration Rights. The rights of Holders to request a Demand Registration or participate in a Piggyback Registration shall expire on March 15, 2007.

ARTICLE XII

EVENTS OF DEFAULTS

XII.1. Events of Default. If any of the following events shall occur and be continuing an "Event of Default" shall be deemed to have occurred:

(a if the Company shall default in the payment of (i) any part of the principal

of any Debenture, 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 any Debenture; when the same shall become due and payable; and in each case such default shall have continued without cure for ten (10) days from the scheduled date of payment of such principal and/or interest;

(b If the Company shall default in the performance of any of the covenants contained in Articles 9 or 10 and in the case of a default under Sections 9.1 through and including 9.8, 9.13, 9.14 or 10.4 (exclusive of Section 10.4(c)), such default shall have continued without cure for thirty days (30) days after written notice (a "Default Notice") is given to the Company with respect to such covenant by any Holder or Holders of the Debentures (the Company to give forthwith to all other Holders of the Debentures at the time outstanding written notice of the receipt of such Default Notice, specifying the default referred to therein);

(c If the Company shall default in the performance of any other material agreement or covenant contained in this Agreement or in any other agreement executed in connection with this Agreement and such default shall not have been remedied to the satisfaction of the Holder or Holders of at least a majority in aggregate principal amount of the Debentures then outstanding, within forty five (45) days after a Default Notice shall have been given to the Company (the Company to give forthwith to all other Holders of Debentures at the time outstanding written notice of the receipt of such Default Notice, specifying the default referred to therein);

(d If any representation or warranty made in this Agreement or in or any certificate delivered pursuant hereto shall prove to have been incorrect 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 Company or a Subsidiary, in excess of $250,000, or which results in such indebtedness, in an aggregate amount (with other defaulted indebtedness) in excess of $750,000 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 Company or its Subsidiaries shall default in the observance or performance of any term or provision of an agreement to which it is a party or by which it is bound which default could reasonably be expected to have a Material Adverse Effect on the Company 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 Company and its Subsidiaries, exceeds an aggregate of $2,000,000 shall be rendered against the Company or any Subsidiary and such judgment shall have continued undischarged or unstayed for sixty (60) days after entry thereof;

(h If the Company 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 Company 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 Company 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 Company 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 Company or any Subsidiary takes corporate action in furtherance of any of the aforesaid purposes or conditions; or

(i (A) Prior to November 30, 1999, the directors and the shareholders of the Company do not (i) approve an amendment to the Certificate of Incorporation of the Company to (a) increase the number of authorized shares of Common Stock from 40,000,000 to 75,000,000 and (b) give the holders of Debentures voting rights as set forth in Section 9.12(A) of this Agreement, and (ii) authorize the issuance by the Company of shares of its Common Stock in excess of twenty percent (20%) of the Company's outstanding shares of the date hereof upon conversion of the Debentures and exercise of the Warrants as set forth in Section 9.12(A) of this Agreement.

XII.2. Remedies.

(a Except as provided in Section 12.2(c) hereof, upon the occurrence of an Event of Default, any Holder or Holders of a majority in aggregate principal amount of the Debentures at the time outstanding may at any time (unless all defaults shall theretofore have been remedied) at its or their option, by written notice or notices to the Company (i) declare all the Debentures 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 the Purchasers under this Agreement or as contemplated hereby due and payable.

(b Notwithstanding anything contained in Section 12.2(a), in the event that at any time after the principal of the Debentures shall so become due and payable and prior to the date of maturity stated in the Debentures all arrears of principal of and interest on the Debentures (with interest at the rate specified in the Debentures on any overdue principal and, to the extent legally enforceable, on any interest overdue) shall be paid by or for the account of the Company, then the holder or holders of at least a majority in aggregate principal amount of the Debentures then outstanding, by written notice or notices to the Company, 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. If any holder of a Debentures shall give any notice or take any other action with respect to a claimed default, the Company, forthwith upon receipt of such notice or obtaining knowledge of such other action will give written notice thereof to all other holders of the Debentures then outstanding, describing such notice or other action and the nature of the claimed default.

(c) Notwithstanding anything to the contrary contained herein, upon the occurrence of an Event of Default under Section 12.1(i)(concerning the failure to obtain shareholder approval of the matters described in such Section) the Purchasers' shall have the right to require the Company to redeem the Debentures at par, together with outstanding interest, plus a default interest payment computed at the annual rate of five percent (5%) accruing from the date of issuance of the Debentures until redeemed by the Company. Upon the occurrence of an Event of Default pursuant to Section 12.1(i), the Purchasers may provide written notice to the Company, in accordance with Section 16.5 hereof, demanding that the Company redeem all or any portion of the Debentures. Not later than fifteen (15) days following the receipt of such notice, the Company shall remit to the Purchasers, against the surrender of the Debentures and the Warrants issued to the Purchaser pursuant to this Agreement, the sum of the principal amount of the Debentures, plus accrued and unpaid interest through the date of redemption computed at the annual rate of five percent (5%), plus a default interest payment computed at the annual rate of five percent (5%) from the date of issuance of the Debentures through and including the date of redemption. The Company's redemption obligations under this Section 12.2(c) are conditioned upon the Purchaser's surrender of the Debentures and Warrants issued pursuant to this Agreement. In the event a Purchaser demands the redemption by the Company of less than the entire principal amount of a Debenture, the Company will issue a new Debenture of like tenor to the Purchaser in a principal amount equal to the unredeemed principal amount of such Debenture.

XII.3. Enforcement. In case any one or more Events of Default shall occur and be continuing, the Holder of a Debenture then outstanding may proceed to protect and enforce the rights of such Holder by an action at law, suit in equity or other appropriate proceeding, whether for the specific performance of any agreement contained herein or in such Debenture 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. Each Holder agrees that it will give written notice to the other Holders prior to instituting any such action. In case of a default in the payment of any principal of or interest on any Debenture, the Company will pay to the Holder thereof such further amount as shall be sufficient to cover the cost and the expenses of collection, including, without limitation, reasonable attorney's fees, expenses and disbursements. No course of dealing and no delay on the part of any Holder of any Debenture in exercising any rights shall operate as a waiver thereof or otherwise prejudice such Holder's rights. No right conferred hereby or by any Debenture upon any Holder thereof shall be exclusive of any other right referred to herein or therein or now available at law in equity, by statute or otherwise.

ARTICLE XIII

AMENDMENT AND WAIVER

This Agreement may not be amended, discharged or terminated (or any provision hereof waived) without the written consent of the Company and the Purchasers. Provided that such written consent of the Company and the Purchasers is given:

(a Holders of at least a majority in aggregate principal amount of the Debentures then outstanding may by written instrument amend or waive any term or condition of

this Agreement relating to the rights or obligations of Holders of Debentures, which amendment or waiver operates for the benefit of such Holders, except that no such amendment or waiver shall (i) change the fixed maturity of any Debentures, the rate or the time of mandatory prepayment of principal thereof or payment of interest thereon, the principal amount thereof, without the consent of the holder of the Debentures so affected, (ii) change the aforesaid percentage of Debentures, the Holders of which are required to consent to any such amendment or waiver, without the consent of the holders of all the Debentures then outstanding or (iii) change the percentage of the amount of the Debentures, the Holders of which may declare the Debentures to be due and payable under Article 12.

The Company and each Holder of a Debenture then or thereafter outstanding shall be bound by any amendment or waiver effected in accordance with the provisions of this Article 13, whether or not such Debenture shall have been marked to indicate such modification, but any Debenture issued thereafter shall bear a notation as to any such modification. Promptly after obtaining the written consent of the holders herein provided, the Company shall transmit a copy of such modification to all of the holders of the Debentures then outstanding.

(b Holders of at least a majority of the Shares then outstanding may by written instrument amend or waive any term or condition of this Agreement relating to the rights or obligations of holders of Shares, which amendment or waiver operates for the benefit of such holders but in no event shall the obligation of any holder of Shares hereunder be increased, except upon the written consent of such holder of Shares.

The Company and each holder of a Share then or thereafter outstanding shall be bound by any amendment or waiver effected in accordance with the provisions of this Article 13, whether or not such Share shall have been marked to indicate such modification, but any Share issued thereafter shall bear a notation as to any such modification. Promptly after obtaining the written consent of the holders herein provided, the Company shall transmit a copy of such modification to all of the holders of the Shares then outstanding.

ARTICLE XIV

EXCHANGE AND REPLACEMENT OF DEBENTURES

XIV.1. Subject to Section 15.2, at any time at the request of any Holder of one or more of the Debentures to the Company at its office provided under Section 16.5, the Company at its expense (except for any transfer tax or any other tax arising out of the exchange) will issue in exchange therefor new Debentures, in such denomination or denominations ($100,000 or any larger multiple of $100,000, plus one Debenture in a lesser denomination, if required) as such Holder may request, in aggregate principal amount equal to the unpaid principal amount of the Debenture or Debentures surrendered and substantially in the form thereof, dated as of the date to which interest has been paid on the Debenture or Debentures surrendered (or, if no interest has yet been so paid thereon, then dated the date of the Debenture or Debentures so surrendered) and payable to such person or persons or order as may be designated by such Holder.

XIV.2. Upon receipt of evidence satisfactory to the Company of the loss, theft,

destruction or mutilation of any Debenture and, in the case of any such loss, theft, or destruction, upon delivery of a bond of indemnity satisfactory to the Company (provided that if the holder is a Purchaser or a financial institution, its own agreement will be satisfactory), or in the case of any such mutilation, upon surrender and cancellation of such Debenture, the Company will issue a new Debenture of like tenor as if the lost, stolen, destroyed or mutilated Debenture were then surrendered for exchange in lieu of such lost, stolen, destroyed or mutilated Debenture.

ARTICLE XV

TRANSFER OF AND PAYMENT OF DEBENTURES

XV.1. Notification of Proposed Sale.

(a Subject to Section 15.1(b), each holder of a Debenture by acceptance thereof agrees that it will give the Company ten (10) days written notice prior to selling or otherwise disposing of such Debenture. No such sale or other disposition shall be made unless (i) the holder shall have supplied to the Company an opinion of counsel for the holder reasonably acceptable to the Company to the effect that no registration under the Securities Act is required with respect to such sale or other disposition, or (ii) an appropriate registration statement with respect to such sale or other disposition shall have been filed by the Company and declared effective by the Commission.

(b If the Holder of a Debenture has obtained an opinion of counsel reasonably acceptable to the Company to the effect that the sale of its Debenture may be made without registration under the Securities Act pursuant to compliance with Rule 144 (or any successor rule under the Securities Act), the holder need not provide the Company with the notice required in Section 15.1(a).

XV.2. Payment. So long as a Purchaser shall be the holder of any Debenture, the Company will make payments of principal and interest to such Purchaser no later than 11 a.m. Eastern Time on the date when such payment is due. Payments shall be made by delivery to such Purchaser at such Purchaser's address furnished to the Company in accordance with this Agreement of a certified or official bank check drawn upon or issued by a bank which is a member of the New York Clearinghouse for banks or by wire transfer to such Purchaser's (or such Purchaser's nominee's) account at any bank or trust company in the United States of America.

ARTICLE XVI

MISCELLANEOUS

XVI.1. Governing Law. This Agreement and the rights of the parties hereunder shall be governed in all respects by the laws of the State of New York wherein the terms of this Agreement were negotiated, without giving effect to its conflict of laws rules.

XVI.2. Survival. Except as specifically provided herein, the representations, warranties, covenants and agreements made herein shall survive (a) any investigation made by the Purchasers and (b) the Closing.

XVI.3. 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.

XVI.4. Entire Agreement. This Agreement (including the Exhibits and Schedules hereto) 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.

XVI.5. Notices, etc. All notices, demands or other communications given hereunder shall be in writing and shall be sufficiently given if transmitted by facsimile or delivered either personally 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, return receipt requested, addressed as follows:

(a if to the Company:

Halsey Drug Co., Inc.
695 N. Perryville Road
Rockford, Illinois
Attention: Mr. Michael Reicher
Chief Executive Officer
Facsimile: (815) 399-9710

(b if to a Purchaser, to the address set forth on Exhibit A attached hereto:

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 parties 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) the Company, shall be delivered to St. John & Wayne, L.L.C., Two Penn Plaza East, Newark, New Jersey 07105-2249 Attn.: John P. Reilly, Esq., or such other address as may be directed and (y) any Purchaser, shall be delivered to Kane Kessler, P.C., 1350 Avenue of the Americas, New York, New York 10019, Attention: Robert L. Lawrence, Esq., Facsimile: (212) 245-3009, or such other address as may be directed.

XVI.6. Delays or Omissions. No delay or omission to exercise any right, power or remedy accruing to any holder of any Securities upon any breach or default of the Company under this Agreement shall impair any such right, power or remedy of such holder 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 any holder of any breach or default under this Agreement, or any waiver on the part of any holder of any provisions or conditions of this 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 Agreement or by law or otherwise afforded to any holder, shall be cumulative and not alternative.

XVI.7. Rights and Obligations; Severability. Unless otherwise expressly provided herein, each Purchaser's rights and obligations hereunder are several rights and obligations, not rights and obligations jointly held with any other person. In case any provision of this 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.

XVI.8. Agent's Fees.

(a The Company hereby (i) represents and warrants that the Company has not retained a finder or broker in connection with the transactions contemplated by this Agreement and (ii) agrees to indemnify and to hold the Purchasers harmless of and from any liability for commission or compensation in the nature of an agent's fee to any broker, person or firm, and the costs and expenses of defending against such liability or asserted liability, including, without limitation, reasonable attorney's fees, arising from any act by the Company or any of the Company's employees or representatives; provided, however, that the Company will have the right to defend against such liability by representative(s) of its own choosing, which representative(s) shall be approved by the Holders of a majority in aggregate principal amount of the Debentures and the Holders of a majority of the Shares (which approval shall not be unreasonably withheld or delayed). In the event that the Company shall fail to undertake the defense within thirty (30) days of any notice of such claim, the Purchasers shall have the right to undertake the defense, compromise or settlement of such claim upon written notice to the Company by holders of a majority in principal amount of the Debentures and the holders of a majority of the Shares and the Company will be responsible for and shall pay all reasonable costs and expenses of defending such liability or asserted liability and any amounts paid in settlement.

(b Each Purchaser (i) severally represents and warrants that it has retained no finder or broker in connection with the transactions contemplated by this Agreement and (ii) hereby severally agrees to indemnify and to hold the Company harmless from any liability for any commission or compensation in the nature of an agent's or finder's fee to any broker or other person or firm (and the costs, including reasonable legal fees, and expenses of defending against such liability or asserted liability) for which such Purchaser, or any of its employees or representatives, are responsible.

XVI.9. Expenses. The Company shall bear its own expenses and legal fees incurred on its behalf with respect to the negotiation, execution and consummation of the transactions contemplated by this Agreement, and the Company will reimburse the Purchasers

for all of the reasonable expenses incurred by the Purchasers and their affiliates with respect to the negotiation, execution and consummation of the transactions contemplated by this Agreement and the transactions contemplated hereby and due diligence conducted in connection therewith, including the fees and disbursements of counsel and auditors for the Purchasers; provided, however, that the amount of such reimbursement shall not exceed $25,000. Such reimbursement shall be paid on the Closing Date.

XVI.10. 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 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 New York and the County of New York shall have exclusive jurisdiction to hear and determine any claims or disputes between the Company and such holders, pertaining directly or indirectly to this 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 16.10 shall not be deemed to preclude the enforcement of any judgment obtained in such forum or the taking of any action under this 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.

XVI.11. Titles and Subtitles. The titles of the articles, sections and subsections of this Agreement are for convenience of reference only and are not to be considered in construing this Agreement.

XVI.12. 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.

If the Purchaser is in agreement with the foregoing the Purchaser shall sign where indicated below and thereupon this letter shall become a binding agreement between such Purchaser and the Company.

HALSEY DRUG CO., INC.

By: /s/ Michael Reicher

Michael Reicher
Chief Executive Officer

Solely as to the Provisions
of Section 9.12(B) hereof

GALEN PARTNERS III, L.P.
By: Claudius, L.L.C., General Partner

By: /s/ Bruce F. Wesson

Bruce F. Wesson
Managing Member

GALEN PARTNERS INTERNATIONAL III, L.P.
By: Claudius, L.L.C., General Manager

By: /s/ Bruce F. Wesson

Bruce F. Wesson
Managing Member

PURCHASERS

ORACLE STRATEGIC PARTNERS, L.P.

By: /s/ Larry Feinberg

GALEN PARTNERS III, L.P.
By: Claudius, L.L.C., General Partner

By: /s/ Bruce F. Wesson

Bruce F. Wesson
Managing Member

GALEN PARTNERS INTERNATIONAL III, L.P.
By: Claudius, L.L.C., General Partner

By: /s/ Bruce F. Wesson

Bruce F. Wesson
Managing Member

GALEN EMPLOYEE FUND III, L.P.
By: Wesson Enterprises, Inc.

By: /s/ Bruce F. Wesson

Bruce F. Wesson
President

/s/ Patrick Coyne

PATRICK COYNE

/s/ Alan Smith

ALAN SMITH

/s/ Michael Weisbrot

MICHAEL WEISBROT

/s/ Susan Weisbrot
- --------------------
SUSAN WEISBROT

/s/ Greg Wood
- --------------------
GREG WOOD

/s/ Dennis Adams
- --------------------
DENNIS ADAMS

/s/ Bernard Selz
- --------------------
BERNARD SELZ

EXHIBIT A

	Name and Address of Purchaser	Principal Amount of Debenture Purchased	$1.404 Warrants	$2.285 Warrants	Purchase Price
1.	Oracle Strategic Partners, L.P.	$ 5,000,000.00	505,050	505,050	$5,000,000.00
2.	Oracle Strategic Partners, L.P.	$10,000,000.00(1)	1,010,100	1,010,100	$10,000,000.00
3.	Galen Partners III, L.P.	$ 5,964,583.09(2)	602,483	602,483	$5,964,583.09
4.	Galen Partners International III, L.P.	$ 539,900.40(3)	54,535	54,535	$539,900.40
5.	Galen Employee Fund III, L.P.	$ 24,424.10(4)	2,467	2,467	$24,424.10
6.	Patrick Coyne	$ 51,178.08(5)	5,169	5,169	$51,178.08
7.	Alan Smith	$ 13,358.08(6)	1,349	1,349	$13,358.08
8.	Michael and Susan Weisbrot	$ 564,446.96(7)	57,015	57,015	$564,446.96
9.	Greg Wood	$ 204,712.33(8)	20,678	20,678	$204,712.33
10.	Dennis Adams	$ 300,000.00	30,303	30,303	$300,000.00
11.	Bernard Selz	$ 200,000.00	20,202	20,202	$200,000.00
	Total	$ 22,862,603.04	2,309,351.00	2,309,351.00	$22,862,603.04

- ------------------------

1 To be funded by Oracle Strategic Partners, L.P. in accordance with the terms of Section 2.1 hereof.

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.

Exhibit 10.73

THIS CONVERTIBLE SENIOR SECURED DEBENTURE AND THE COMMON STOCK ISSUABLE UPON CONVERSION HEREOF HAVE NOT BEEN REGISTERED UNDER THE SECURITIES ACT OF 1933, AS AMENDED (THE "ACT") NOR UNDER ANY STATE SECURITIES LAW AND MAY NOT BE PLEDGED, SOLD, ASSIGNED, HYPOTHECATED OR OTHERWISE TRANSFERRED UNTIL (1) A REGISTRATION STATEMENT WITH RESPECT THERETO IS EFFECTIVE UNDER THE ACT AND ANY APPLICABLE STATE SECURITIES LAW OR (2) THE COMPANY RECEIVES AN OPINION OF COUNSEL TO THE COMPANY OR OTHER COUNSEL TO THE HOLDER OF SUCH DEBENTURE REASONABLY SATISFACTORY TO THE COMPANY THAT SUCH DEBENTURE AND/OR COMMON STOCK MAY BE PLEDGED, SOLD, ASSIGNED, HYPOTHECATED OR TRANSFERRED WITHOUT AN EFFECTIVE REGISTRATION STATEMENT UNDER THE ACT OR APPLICABLE STATE SECURITIES LAWS.

HALSEY DRUG CO., INC.
5% CONVERTIBLE SENIOR SECURED DEBENTURE
DUE MARCH 15, 2003

$5,000,000 No. N-1
May 28, 1999

HALSEY DRUG CO., INC., a corporation organized under the laws of the State of New York (the "Company"), for value received, hereby promises to pay to ORACLE STRATEGIC PARTNERS, L.P., or registered assigns (the "Payee" or "Holder") upon due presentation and surrender of this Debenture, on March 15, 2003 (the "Maturity Date"), the principal amount of Five Million Dollars ($5,000,000) and accrued interest thereon as hereinafter provided.

This Debenture was issued by the Company pursuant to a certain Debenture and Warrant Purchase Agreement dated as of May 26, 1999 among the Company and certain persons, including the Payee (together with the Schedules and Exhibits thereto, the "Purchase Agreement") relating to the purchase and sale of 5% Convertible Senior Secured Debentures maturing March 15, 2003 (the "Debentures") in the aggregate principal amount of $22,862,603.04. The holders of such Debentures are referred to hereinafter as the "Holders." The Payee is entitled to the benefits of the Purchase Agreement, including, without limitation, the rights on the occurrence of an Event of Default (as defined in the Purchase Agreement). Reference is made to the Purchase Agreement with respect to certain additional rights of the Holder and obligations of the Company not set forth herein.

ARTICLE I

PAYMENT OF PRINCIPAL AND INTEREST; METHOD OF PAYMENT

1.1 Payment of the principal and accrued interest on this Debenture shall be made in such coin or currency of the United States of America as at the time of payment shall be legal tender for the payment of public and private debts. Interest (computed on the basis of a 360-day year of twelve 30-day months) on the unpaid portion of said principal amount from time to time outstanding shall be paid by the Company at the rate of five percent (5%) per annum (the "Stated Interest Rate"), in like coin and currency, payable to the Payee in three (3) month intervals on each January 1, April 1,

July 1 and October 1 during the term of this Debenture (commencing July 1, 1999) (an "Interest Payment Date") and on the Maturity Date. Both principal hereof and interest thereon are payable at the Holder's address above or such other address as the Holder shall designate from time to time by written notice to the Company. The Company will pay or cause to be paid all sums becoming due hereon for principal and interest by check, sent to the Holder's above address or to such other address as the Holder may designate for such purpose from time to time by written notice to the Company, without any requirement for the presentation of this Debenture or making any notation thereon, except that the Holder hereof agrees that payment of the final amount due shall be made only upon surrender of this Debenture to the Company for cancellation. Prior to any sale or other disposition of this instrument, the Holder hereof agrees to endorse hereon the amount of principal paid hereon and the last date to which interest has been paid hereon and to notify the Company of the name and address of the transferee.

1.2 In the event any payment of principal or interest or both shall remain unpaid for a period of ten (10) days or more, a late charge equivalent to five (5%) percent of each installment shall be charged. Interest on the indebtedness evidenced by this Debenture after default or maturity accelerated shall be due and payable at the rate of seven (7%) percent per annum, subject to the limitations of applicable law.

1.3 If this Debenture or any installment hereof becomes due and payable on a Saturday, Sunday or public holiday under the laws of the State of New York, the due date hereof shall be extended to the next succeeding full business day and interest shall be payable at the rate of five (5%) percent per annum during such extension. All payments received by the Holder shall be applied first to the payment of all accrued interest payable hereunder.

ARTICLE II

SECURITY

2.1 The obligations of the Company under this Debenture are secured pursuant to security interests on and collateral assignments of, assets, tangible and intangible, of the Company granted by the Company to the Payee pursuant to a security agreement dated as of May 26, 1999 and collateral assignments referred to in the Purchase Agreement. In addition, each of Houba, Inc. ("Houba") and Halsey Pharmaceuticals, Inc., each a wholly-owned subsidiary of the Company (individually a "Guarantor" and collectively, the "Guarantors"), has executed in favor of the Holder a certain Continuing Unconditional Guaranty, dated as of May 26, 1999, guaranteeing the full and unconditional payment when due of the amounts payable by the Company to the Holder pursuant to the terms of this Debenture (each the "Guaranty"). The obligations of each Guarantor under its Guaranty are secured pursuant to security interests on and collateral assignments of, assets, tangible and intangible, of such Guarantor granted by the Guarantor to the Payee pursuant to a security agreement of even date herewith and collateral assignments referred to in the Purchase Agreement. The obligations of Houba under its Guaranty are also secured pursuant to a Mortgage on real property located at 16235 State Road 17, Culver, Indiana.

ARTICLE III

CONVERSION

3.1 Conversion at Option of Holder. (a) Except as set forth in Section 3.1(b) hereof, at any time and from time to time on and after May 26, 1999 (the "Initial Conversion Date") until the earlier of (i) the Maturity Date or (ii) the conversion of the Debenture in accordance with Section 3.2 hereof, this Debenture is convertible in whole or in part at the Holder's option into shares of Common Stock of the Company upon surrender of this Debenture, at the office of the Company, accompanied by a written notice of conversion in the form of Attachment II hereto, or otherwise in form reasonably satisfactory to the Company duly executed by the registered Holder or its duly authorized attorney. This Debenture is convertible on or after the Initial Conversion Date into shares of Common Stock at a price per share of Common Stock equal to $1.404 per share (the "Conversion Price"). Interest shall accrue to and including the day prior to the date of conversion and shall be paid on the last day of the month in which conversion rights hereunder are exercised. No fractional shares or scrip representing fractional shares will be issued upon any conversion, but an adjustment in cash will be made, in respect of any fraction of a share which would otherwise be issuable upon the surrender of this Debenture for conversion. The Conversion Price is subject to adjustment as provided in Section 3.5 and Section 3.7 hereof. As soon as practicable following conversion and upon the Holder's compliance with the conversion procedure described in Section 3.3 hereof, the Company shall deliver a certificate for the number of full shares of Common Stock issuable upon conversion and a check for any fractional share and, in the event the Debenture is converted in part, a new Debenture of like tenor in the principal amount equal to the remaining principal balance of this Debenture after giving effect to such partial conversion.

(b) Notwithstanding anything to the contrary contained herein, in no event shall this Debenture be convertible into, and the Company shall have no obligation to issue, an amount exceeding 484,349 shares of the Company's Common Stock until such time as the Company's shareholders shall have approved the issuance of shares of Common Stock in an amount exceeding 19.9% of the Company's outstanding Common Stock (determined as of the date hereof) at a price less than the current fair market value of the Common Stock upon the conversion of the Debentures and exercise of the Warrants ("Shareholder Approval"). Immediately upon receipt of Shareholder Approval, this Debenture shall be convertible in whole or in part into shares of the Company's Common Stock as provided in Sections 3.1 and 3.2 hereof. In accordance with the provisions of Section 9.12 of the Purchase Agreement, the Company covenants to seek Shareholder Approval as required pursuant to this Section 3.1(b). Notwithstanding anything to the contrary contained herein, upon the occurrence of an Event of Default under Section 12.1(i) of the Purchase Agreement (concerning the failure to obtain shareholder approval of the matters described in such Section) the Purchasers' shall have the right to require the Company, upon notice, to redeem the Debentures at par, together with outstanding interest, plus a default interest payment computed at the annual rate of five percent (5%) accruing from the date of issuance of the Debentures until redeemed by the Company. Not later than fifteen (15) days following the receipt of such notice, the Company shall remit to the Purchasers, against the surrender of the Debentures and the Warrants issued to the Purchaser pursuant to this Agreement, the sum of the principal amount of the Debentures, plus accrued and unpaid interest through the date of redemption computed at the annual rate of five percent (5%), plus a default interest payment computed at the annual rate of five percent (5%) from the date of issuance of the Debentures through and including the date of redemption. The Company's redemption obligations under Section 12.2(c) of the Purchase Agreement are conditioned upon the Purchaser's surrender of the

Debentures and Warrants issued pursuant to this Agreement. In the event a Purchaser demands the redemption by the Company of less than the entire principal amount of a Debenture, the Company will issue a new Debenture of like tenor to the Purchaser in a principal amount equal to the unredeemed principal amount of such Debenture.

3.2 Conversion at Option of the Company. Provided that an Event of Default as provided in Section 12.1(a) of the Purchase Agreement (relating to the failure to pay principal and interest under the Debentures) shall not have occurred and then be continuing and subject to the terms of Section 3.1(b) hereof, in the event that either (a) following the second anniversary of May 26, 1999, the closing price per share of the Company's Common Stock on the American Stock Exchange ("AMEX") or the NASDAQ National Market ("NNM") or such other exchange as the Shares may then be listed exceeds $4.75 per share for each of twenty (20) consecutive trading days or (b) following the third anniversary of May 26, 1999, the closing price per share of the Company's Common Stock on the AMEX or NNM or such other exchange as the Share may then be listed exceeds $7.25 per share for each of twenty (20) consecutive trading days, then at any time thereafter until the Maturity Date the Company may upon written notice to the Holders of all Debentures (the "Mandatory Conversion Notice") require that all, but not less than all, of the outstanding principal amount of the Debentures be converted into shares of Common Stock at a price per share equal to the Conversion Price (as such Conversion Price may be adjusted as provided in Sections 3.5 and 3.7 hereof). The Mandatory Conversion Notice shall state (1) the date fixed for conversion (the "Conversion Date") (which date shall not be prior to the date the Mandatory Conversion Notice is given), (2) any disclosures required by law, (3) the trading dates and closing prices of the Common Stock giving rise to the Company's option to require conversion of the Debenture, (4) that the Debentures shall cease to accrue interest after the day immediately preceding the Conversion Date, (5) the place where the Debentures shall be delivered and (6) any other instructions that Holders must follow in order to tender their Debentures in exchange for certificates for Common Stock. No failure to mail such notice nor any defect therein or in the mailing thereof shall affect the validity of the proceedings for such conversion, except as to a Holder (x) to whom notice was not mailed or (y) whose notice was defective. An affidavit of the Secretary or an Assistant Secretary of the Company or an agent employed by the Company that notice of conversion has been mailed postage prepaid to the last address of the Holder appearing on the Debenture registry books kept by the Company shall, in the absence of fraud, be prima facie evidence of the facts stated therein. On and after the Conversion Date, except as provided in the next two sentences, Holders of the Debentures shall have no further rights except to receive, upon surrender of the Debentures, a certificate or certificates for the number of shares of Common Stock as to which the Debenture shall have been converted. Interest shall accrue to and including the day prior to the Conversion Date and shall be paid on the last day of the month in which Conversion Date occurs. No fractional shares or scrip representing fractional shares will be issued upon any conversion, but an adjustment in cash will be made, in respect of any fraction of a share which would otherwise be issuable upon the surrender of this Debenture for conversion.

3.3 Registration of Transfer; Conversion Procedure. The Company shall maintain books for the transfer and registration of the Debentures. Upon the transfer of any

Debenture in accordance with the provisions of the Purchase Agreement, the Company shall issue and register the Debenture in the names of the new holders. The Debentures shall be signed manually by the Chairman, Chief Executive Officer, President or any Vice President and the Secretary or Assistant Secretary of the Company. The Company shall convert, from time to time, any outstanding Debentures upon the books to be maintained by the Company for such purpose upon surrender thereof for conversion properly endorsed and, in the case of a conversion pursuant to Section 3.1 hereof, accompanied by a properly completed and executed Conversion Notice attached hereto as Attachment II. Subject to the terms of this Debenture, upon surrender of this Debenture the Company shall issue and deliver with all reasonable dispatch to or upon the written order of the Holder of such Debenture and in such name or names as such Holder may designate, a certificate or certificates for the number of full shares of Common Stock due to such Holder upon the conversion of this Debenture. Such certificate or certificates shall be deemed to have been issued and any person so designated to be named therein shall be deemed to have become the Holder of record of such Shares as of the date of the surrender of this Debenture.

3.4 Company to Provide Common Stock. The Holder acknowledges that the Company has no authorized and unreserved Shares available to reserve for issuance upon the conversion of the Debentures. In accordance with the provisions of Section 9.12 of the Purchase Agreement, the Company covenants to seek the approval of its shareholders to amend its Certificate of Incorporation to increase its authorized shares from 40,000,000 to 75,000,000 shares of Common Stock and to provide voting rights to the Holders on an as converted basis. Promptly upon receipt of shareholder approval to amend its certificate of incorporation to increase its authorized shares, the Company shall reserve out of its authorized but unissued common stock a sufficient number of shares to permit the conversion of the Debentures in full. The shares of Common Stock which may be issued upon the conversion of the Debentures shall be fully paid and non-assessable and free of preemptive rights. The Company will comply with all securities laws regulating the offer and delivery of the Shares upon conversion of the Debentures and will list such shares on each national securities exchange upon which the Common Stock is listed.

3.5 Dividends; Reclassifications, etc. In the event that the Company shall, at any time prior to the earlier to occur of (i) exercise of conversion rights hereunder and (ii) the Maturity Date: (i) declare or pay to the holders of the Common Stock a dividend payable in any kind of shares of capital stock of the Company; or (ii) change or divide or otherwise reclassify its Common Stock into the same or a different number of shares with or without par value, or in shares of any class or classes; or (iii) transfer its property as an entirety or substantially as an entirety to any other company or entity; or (iv) make any distribution of its assets to holders of its Common Stock as a liquidation or partial liquidation dividend or by way of return of capital; then, upon the subsequent exercise of conversion rights, the Holder thereof shall receive, in addition to or in substitution for the shares of Common Stock to which it would otherwise be entitled upon such exercise, such additional shares of stock or scrip of the Company, or such reclassified shares of stock of the Company, or such shares of the securities or property of the Company resulting from transfer, or such assets of the Company, which it would have been entitled to receive had it exercised these conversion rights prior to the happening of any of the foregoing events.

3.6 Notice to Holder. If, at any time while this Debenture is outstanding, the

Company shall pay any dividend payable in cash or in Common Stock, shall offer to the holders of its Common Stock for subscription or purchase by them any shares of stock of any class or any other rights, shall enter into an agreement to merge or consolidate with another corporation, shall propose any capital reorganization or reclassification of the capital stock of the Company, including any subdivision or combination of its outstanding shares of Common Stock or there shall be contemplated a voluntary or involuntary dissolution, liquidation or winding up of the Company, the Company shall cause notice thereof to be mailed to the registered Holder of this Debenture at its address appearing on the registration books of the Company, at least thirty (30) days prior to the record date as of which holders of Common Stock shall participate in such dividend, distribution or subscription or other rights or at least thirty (30) days prior to the effective date of the merger, consolidation, reorganization, reclassification or dissolution. If, at any time prior to the earlier of (a) the Maturity Date, or (b) the Conversion of the Debenture, the number of outstanding shares of Common Stock is (i) increased by a stock dividend payable in shares of Common Stock or by a subdivision or split up of shares of Common Stock, or (ii) decreased by a combination of shares of Common Stock, then, simultaneously with the occurrence of such event, the Conversion Price shall be adjusted automatically to a new amount equal to the product of (A) the Conversion Price in effect on such record date and (B) the quotient obtained by dividing (x) the number of shares of Common Stock outstanding on such record date (without giving effect to the events referred to in the foregoing clauses (i) or (ii)) by (y) the number of shares of Common Stock which would be outstanding immediately after the event referred to in the foregoing clauses (i) or (ii).

3.7 Adjustments to Conversion Price. In order to prevent dilution of the conversion right granted hereunder, the Conversion Price shall be subject to adjustment from time to time in accordance with this Section 3.7. Upon each adjustment of the Conversion Price pursuant to this Section 3.7, the Holder of this Debenture shall thereafter be entitled to acquire upon conversion under Section 3.1 or Section 3.2, at the Applicable Conversion Price (as hereinafter defined), the number of shares of Common Stock obtainable by multiplying the Conversion Price in effect immediately prior to such adjustment by the number of shares of Common Stock acquirable immediately prior to such adjustment and dividing the product thereof by the Applicable Conversion Price resulting from such adjustment.

The Conversion Price in effect at the time of the exercise of conversion rights hereunder set forth in Section 3.1 shall be subject to adjustment from time to time as follows:

(a) If at any time after the date of issuance hereof the Company shall grant or issue any shares of Common Stock, or grant or issue any rights or options for the purchase of, or stock or other securities convertible into, Common Stock (such convertible stock or securities being herein collectively referred to as "Convertible Securities") other than:

(i) shares issued in a transaction described in subsection (b) of this Section 3.7; or

(ii) shares issued, subdivided or combined in transactions described in Section 3.5 if and to the extent that the number of shares of Common Stock received

upon conversion of this Debenture shall have been previously adjusted pursuant to Section 3.5 as a result of such issuance, subdivision or combination of such securities;

for a consideration per share which is less than the Fair Market Value (as hereinafter defined) of the Common Stock, then the Conversion Price in effect immediately prior to such issuance or sale (the "Applicable Conversion Price") shall, and thereafter upon each issuance or sale for a consideration per share which is less than the Fair Market Value of the Common Stock, the Applicable Conversion Price shall, simultaneously with such issuance or sale, be adjusted, so that such Applicable Conversion Price shall equal a price determined by multiplying the Applicable Conversion Price by a fraction, the numerator of which shall be:

(A) the sum of (x) the total number of shares of Common Stock outstanding when the Applicable Conversion Price became effective, plus (y) the number of shares of Common Stock which the aggregate consideration received, as determined in accordance with subsection 3.7(c) for the issuance or sale of such additional Common Stock or Convertible Securities deemed to be an issuance of Common Stock as provided in subsection 3.7(d), would purchase (including any consideration received by the Company upon the issuance of any shares of Common Stock since the date the Applicable Conversion Price became effective not previously included in any computation resulting in an adjustment pursuant to this Section 3.7(a)) at the Fair Market Value of the Common Stock; and the denominator of which shall be

(B) the total number of shares of Common Stock outstanding (or deemed to be outstanding as provided in subsection 3.7(d) hereof) immediately after the issuance or sale of such additional shares.

For purposes of this Section 3.7, "Fair Market Value" shall mean the average of the closing price of the Common Stock for each of the twenty (20) consecutive trading days prior to such issuance or sale on the principal national securities exchange on which the Common Stock is traded, or if shares of Common Stock are not listed on a national securities exchange during such period, the closing price per share as reported by the National Association of Securities Dealers Automatic Quotation System ("NASDAQ") National Market System if the shares are quoted on such system during such period, or the average of the bid and asked prices of the Common Stock in the over-the-counter market at the close of trading during such period if the shares are not traded on an exchange or listed on the NASDAQ National Market System, or if the Common Stock is not traded on a national securities exchange or in the over-the-counter market, the fair market value of a share of Common Stock during such period as determined in good faith by the Board of Directors.

If, however, the Applicable Conversion Price thus obtained would result in the issuance of a lesser number of shares upon conversion than would be issued at the initial Conversion Price specified in Section 3.1, as appropriate, the Applicable Conversion Price shall be such initial Conversion Price.

Upon each adjustment of the Conversion Price pursuant to this subsection (a), the

total number of shares of Common Stock into which this Debenture shall be convertible shall be such number of shares (calculated to the nearest tenth) purchasable at the Applicable Conversion Price multiplied by a fraction, the numerator of which shall be the Conversion Price in effect immediately prior to such adjustment and the denominator of which shall be the exercise price in effect immediately after such adjustment.

(b) Anything in this Section 3.7 to the contrary notwithstanding, no adjustment in the Conversion Price shall be made in connection with:

(i) the grant, issuance or exercise of any Convertible Securities pursuant to the Company's qualified or non-qualified Employee Stock Option Plans or any other bona fide employee benefit plan or incentive arrangement, adopted or approved by the Company's Board of Directors or approved by the Company's shareholders, as may be amended from time to time, or under any other bona fide employee benefit plan hereafter adopted by the Company's Board of Directors; or

(ii) the grant, issuance or exercise of any Convertible Securities in connection with the hire or retention of any officer, director or key employee of the Company, provided such grant is approved by the Company's Board of Directors; or

(iii) the issuance of any shares of Common Stock pursuant to the grant or exercise of Convertible Securities outstanding as of the date hereof (exclusive of any subsequent amendments thereto).

(c) For the purpose of subsection 3.7(a), the following provisions shall also be applied:

(i) In case of the issuance or sale of additional shares of Common Stock for cash, the consideration received by the Company therefor shall be deemed to be the amount of cash received by the Company for such shares, before deducting therefrom any commissions, compensation or other expenses paid or incurred by the Company for any underwriting of, or otherwise in connection with, the issuance or sale of such shares.

(ii) In the case of the issuance of Convertible Securities, the consideration received by the Company therefor shall be deemed to be the amount of cash, if any, received by the Company for the issuance of such rights or options, plus the minimum amounts of cash and fair value of other consideration, if any, payable to the Company upon the exercise of such rights or options or payable to the Company upon conversion of such Convertible Securities.

(iii) In the case of the issuance of shares of Common Stock or Convertible Securities for a consideration in whole or in part, other than cash, the consideration other than cash shall be deemed to be the fair market value thereof as reasonably determined in good faith by the Board of Directors of the Company (irrespective of

accounting treatment thereof); provided, however, that if such consideration consists of the cancellation of debt issued by the Company, the consideration shall be deemed to be the amount the Company received upon issuance of such debt (gross proceeds) plus accrued interest and, in the case of original issue discount or zero coupon indebtedness, accrued value to the date of such cancellation, but not including any premium or discount at which the debt may then be trading or which might otherwise be appropriate for such class of debt.

(iv) In case of the issuance of additional shares of Common Stock upon the conversion or exchange of any obligations (other than Convertible Securities), the amount of the consideration received by the Company for such Common Stock shall be deemed to be the consideration received by the Company for such obligations or shares so converted or exchanged, before deducting from such consideration so received by the Company any expenses or commissions or compensation incurred or paid by the Company for any underwriting of, or otherwise in connection with, the issuance or sale of such obligations or shares, plus any consideration received by the Company in connection with such conversion or exchange other than a payment in adjustment of interest and dividends. If obligations or shares of the same class or series of a class as the obligations or shares so converted or exchanged have been originally issued for different amounts of consideration, then the amount of consideration received by the Company upon the original issuance of each of the obligations or shares so converted or exchange shall be deemed to be the average amount of the consideration received by the Company upon the original issuance of all such obligations or shares. The amount of consideration received by the Company upon the original issuance of the obligations or shares so converted or exchanged and the amount of the consideration, if any, other than such obligations or shares, received by the Company upon such conversion or exchange shall be determined in the same manner as provided in paragraphs (i) and (ii) above with respect to the consideration received by the Company in case of the issuance of additional shares of Common Stock or Convertible Securities.

(v) In the case of the issuance of additional shares of Common Stock as a dividend, the aggregate number of shares of Common Stock issued in payment of such dividend shall be deemed to have been issued at the close of business on the record date fixed for the determination of stockholders entitled to such dividend and shall be deemed to have been issued without consideration; provided, however, that if the Company, after fixing such record date, shall legally abandon its plan to so issue Common Stock as a dividend, no adjustment of the Applicable Conversion Price shall be required by reason of the fixing of such record date.

(d) For purposes of the adjustment provided for in subsection 3.7(a) above, if at any time the Company shall issue any Convertible Securities, the Company shall be deemed to have issued at the time of the issuance of such Convertible Securities the maximum number of shares of Common Stock issuable upon conversion of the total amount of such Convertible Securities.

(e) On the expiration, cancellation or redemption of any Convertible Securities, the Conversion Price then in effect hereunder shall forthwith be readjusted to such Conversion Price as would have been obtained (a) had the adjustments made upon the issuance or sale of such expired, canceled or redeemed Convertible Securities been made upon the basis of the issuance of only the number of shares of Common Stock theretofore actually delivered upon the exercise or conversion of such Convertible Securities (and the total consideration received therefor) and (b) had all subsequent adjustments been made on only the basis of the Conversion Price as readjusted under this subsection 3.7(e) for all transactions (which would have affected such adjusted Conversion Price) made after the issuance or sale of such Convertible Securities.

(f) Anything in this Section 3.7 to the contrary notwithstanding, no adjustment in the Conversion Price shall be required unless such adjustment would require an increase or decrease of at least 1% in such Conversion Price; provided, however, that any adjustments which by reason of this subsection 3.7(f) are not required to be made shall be carried forward and taken into account in making subsequent adjustments. All calculations under this Section 3.7 shall be made to the nearest cent.

(g) Upon any adjustment of any Conversion Price, then and in each such case the Company shall promptly deliver a notice to the registered Holder of this Debenture, which notice shall state the Conversion Price resulting from such adjustment, setting forth in reasonable detail the method of calculation and the facts upon which such calculation is based.

3.8 Reorganization of the Company. If the Company is a party to a merger or other transaction which reclassifies or changes its outstanding Common Stock, upon consummation of such transaction this Debenture shall automatically become convertible into the kind and amount of securities, cash or other assets which the Holder of this Debenture would have owned immediately after such transaction if the Holder had converted this Debenture at the Conversion Price in effect immediately before the effective date of the transaction. Concurrently with the consummation of such transaction, the person obligated to issue securities or deliver cash or other assets upon conversion of this Debenture shall execute and deliver to the Holder a supplemental Debenture so providing and further providing for adjustments which shall be as nearly equivalent as may be practical to the adjustments provided in this Article 3. The successor Company shall mail to the Holder a notice describing the supplemental Debenture.

If securities deliverable upon conversion of this Debenture, as provided above, are themselves convertible into the securities of an affiliate of a corporation formed, surviving or otherwise affected by the merger or other transaction, that issuer shall join in the supplemental Debenture which shall so provide. If this section applies, Section 3.5 does not apply.

ARTICLE IV

MISCELLANEOUS

4.1 Default. Upon the occurrence of any one or more of the events of default specified or referred to in the Purchase Agreement or in the other documents or instruments

executed in connection therewith, all amounts then remaining unpaid on this Debenture may be declared to be immediately due and payable as provided in the Purchase Agreement.

4.2 Collection Costs. In the event that this Debenture shall be placed in the hands of an attorney for collection by reason of any event of default hereunder, the undersigned agrees to pay reasonable attorney's fees and disbursements and other reasonable expenses incurred by the Holder in connection with the collection of this Debenture.

4.3 Rights Cumulative. The rights, powers and remedies given to the Payee under this Debenture shall be in addition to all rights, powers and remedies given to it by virtue of the Purchase Agreement, any document or instrument executed in connection therewith, or any statute or rule of law.

4.4 No Waivers. Any forbearance, failure or delay by the Payee in exercising any right, power or remedy under this Debenture, the Purchase Agreement, any documents or instruments executed in connection therewith or otherwise available to the Payee shall not be deemed to be a waiver of such right, power or remedy, nor shall any single or partial exercise of any right, power or remedy preclude the further exercise thereof.

4.5 Amendments in Writing. No modification or waiver of any provision of this Debenture, the Purchase Agreement or any documents or instruments executed in connection therewith shall be effective unless it shall be in writing and signed by the Payee, and any such modification or waiver shall apply only in the specific instance for which given.

4.6 Governing Law. This Debenture and the rights and obligations of the parties hereto, shall be governed, construed and interpreted according to the laws of the State of New York, without giving effect to its conflicts of laws rules wherein it was negotiated and executed, and the undersigned consents and agrees that the State and Federal Courts which sit in the State of New York, County of New York shall have exclusive jurisdiction of all controversies and disputes arising hereunder.

4.7 No Counterclaims. The undersigned waives the right to interpose counterclaims or set-offs of any kind and description in any litigation arising hereunder and waives the right in any litigation with the Payee (whether or not arising out of or relating to this Debenture) to trial by jury.

4.8 Successors. The term "Payee" and "Holder" as used herein shall be deemed to include the Payee and its successors, endorsees and assigns.

4.9 Certain Waivers. The Company hereby waives presentment, demand for payment, protest, notice of protest and notice of non-payment hereof.

4.10 Stamp Tax. The Company will pay any documentary stamp taxes attributable to the initial issuance of the Common Stock issuable upon the conversion of this

Debenture; provided, however, that the Company shall not be required to pay any tax or taxes which may be payable in respect of any transfer involved in the issuance or delivery of any certificates for the Common Stock in a name other than that of the Holder in respect of which such Common Stock is issued, and in such case the Company shall not be required to issue or deliver any certificate for the Common Stock until the person requesting the same has paid to the Company the amount of such tax or has established to the Company's satisfaction that such tax has been paid.

4.11 Mutilated, Lost, Stolen or Destroyed Debentures. In case this Debenture shall be mutilated, lost, stolen or destroyed, the Company shall issue and deliver in exchange and substitution for and upon cancellation of the mutilated Debenture, or in lieu of and substitution for the Debenture, mutilated, lost, stolen or destroyed, a new Debenture of like tenor and representing an equivalent right or interest, but only upon receipt of evidence reasonably satisfactory to the Company of such loss, theft or destruction and an indemnity, if requested, also reasonably satisfactory to it.

4.12 Maintenance of Office. The Company covenants and agrees that so long as this Debenture shall be outstanding, it will maintain an office or agency in New York (or such other place as the Company may designate in writing to the holder of this Debenture) where notices, presentations and demands to or upon the Company in respect of this Debenture may be given or made.

IN WITNESS WHEREOF, Halsey Drug Co., Inc. has caused this Debenture to be signed by its President and to be dated the day and year first above written.

ATTEST [SEAL]

HALSEY DRUG CO., INC.

By: /s/ Michael Reicher

- ----------

Name: Michael Reicher
Title: President

ATTACHMENT I

Assignment

For value received, the undersigned hereby assigns subject to the provisions of Section of the Purchase Agreement, to _____ $_____ principal amount of the 5% Convertible Senior Secured Debenture due March 15, 2003 evidenced hereby and hereby irrevocably appoint _____ attorney to transfer the Debenture on the books of the within named corporation with full power of substitution in the premises.

Dated:

In the presence of:

- ---------- ----------

ATTACHMENT II

CONVERSION NOTICE

TO: HALSEY DRUG CO., INC.

The undersigned holder of this Debenture hereby irrevocably exercises the option to convert $ principal amount of such Debenture (which may be less than the stated principal amount thereof) into shares of Common Stock of Halsey Drug Co., Inc., in accordance with the terms of such Debenture, and directs that the shares of Common Stock issuable and deliverable upon such conversion, together with a check (if applicable) in payment for any fractional shares as provided in such Debenture, be issued and delivered to the undersigned unless a different name has been indicated below. If shares of Common Stock are to be issued in the name of a person other than the undersigned holder of such Debenture, the undersigned will pay all transfer taxes payable with respect thereto.

Name and address of Holder

Signature of Holder

Principal amount of Debenture to be converted $

If shares are to be issued otherwise then to the holder:

- ----------

Name of Transferee

Address of Transferee

Social Security Number of Transferee

WARRANT TO PURCHASE
COMMON STOCK, PAR VALUE $.01 PER SHARE

OF

HALSEY DRUG CO., INC.

THIS WARRANT AND THE COMMON STOCK ISSUABLE UPON EXERCISE HEREOF HAVE NOT BEEN REGISTERED UNDER THE SECURITIES ACT OF 1933, AS AMENDED (THE "ACT") NOR UNDER ANY STATE SECURITIES LAW AND MAY NOT BE PLEDGED, SOLD, ASSIGNED, HYPOTHECATED OR OTHERWISE TRANSFERRED UNTIL (1) A REGISTRATION STATEMENT WITH RESPECT THERETO IS EFFECTIVE UNDER THE ACT AND ANY APPLICABLE STATE SECURITIES LAW OR (2) THE COMPANY RECEIVES AN OPINION OF COUNSEL TO THE COMPANY OR OTHER COUNSEL TO THE HOLDER OF SUCH WARRANT REASONABLY SATISFACTORY TO THE COMPANY THAT SUCH WARRANT AND/OR COMMON STOCK MAY BE PLEDGED, SOLD, ASSIGNED, HYPOTHECATED OR TRANSFERRED WITHOUT AN EFFECTIVE REGISTRATION STATEMENT UNDER THE ACT OR APPLICABLE STATE SECURITIES LAWS.

This certifies that, for value received, ORACLE STRATEGIC PARTNERS, L.P., or registered assigns ("Warrantholder"), is entitled to purchase from HALSEY DRUG CO., INC. (the "Company"), subject to the provisions of this Warrant, at any time during the Exercise Period (as hereinafter defined) 505,050 shares of the Company's Common Stock, par value $.01 per share ("Warrant Shares"). The purchase price payable upon the exercise of this Warrant shall be $1.404 per Warrant Share. The purchase price and the number of Warrant Shares which the Warrantholder is entitled to purchase are subject to adjustment upon the occurrence of the contingencies set forth in this Warrant, and as adjusted from time to time, such purchase price is hereinafter referred to as the "Warrant Price."

For purposes of this Warrant, the term "Exercise Period" means the period commencing on the date of issuance of this Warrant and ending on the seventh anniversary of such date.

This Warrant is subject to the following terms and conditions:

1. Exercise of Warrant.

(a) Subject to the terms of Section 1(e) hereof, this Warrant may be exercised in whole or in part but not for a fractional share. Upon delivery of this Warrant at the offices of the Company or at such other address as the Company may designate by notice in writing to the registered holder hereof with the Subscription Form annexed hereto duly executed, accompanied by payment of the Warrant Price for the number of Warrant Shares purchased (in

cash, by certified, cashier's or other check acceptable to the Company, by Common Stock or other securities of the Company having a Market Value (as hereinafter defined) equal to the aggregate Warrant Price for the Warrant Shares to be purchased, or any combination of the foregoing), the registered holder of this Warrant shall be entitled to receive a certificate or certificates for the Warrant Shares so purchased. Such certificate or certificates shall be promptly delivered to the Warrantholder. Upon any partial exercise of this Warrant, the Company shall execute and deliver a new Warrant of like tenor for the balance of the Warrant Shares purchasable hereunder.

(b) In lieu of exercising this Warrant pursuant to Section 1(a), the holder may elect to receive shares of Common Stock equal to the value of this Warrant determined in the manner described below (or any portion thereof remaining unexercised) upon delivery of this Warrant at the offices of the Company or at such other address as the Company may designate by notice in writing to the registered holder hereof with the Notice of Cashless Exercise Form annexed hereto duly executed. In such event the Company shall issue to the holder a number of shares of the Company's Common Stock computed using the following formula:

$$X = \frac{Y\,(A-B)}{A}$$

Where X = the number of shares of Common Stock to be issued to the holder.

Y = the number of shares of Common Stock purchasable under this Warrant (at the date of such calculation).

A = the Market Value of the Company's Common Stock on the business day immediately preceding the day on which the Notice of Cashless Exercise is received by the Company.

B = Warrant Price (as adjusted to the date of such calculation).

(c) The Warrant Shares deliverable hereunder shall, upon issuance, be fully paid and non-assessable and the Company agrees that at all times during the term of this Warrant it shall cause to be reserved for issuance such number of shares of its Common Stock as shall be required for issuance and delivery upon exercise of this Warrant.

(d) For purposes of Section 1(b) of this Warrant, the Market Value of a share of Common Stock on any date shall be equal to (A) the closing sale price per share as published by a national securities exchange on which shares of Common Stock are traded (an "Exchange") on such date or, if there is no sale of Common Stock on such date, the average of the bid and asked prices on such Exchange at the close of trading on such date or, (B) if shares of Common Stock are not listed on an Exchange on such date, the closing price per share as published on the National Association of Securities Dealers Automatic Quotation System ("NASDAQ") National Market System if the shares are quoted on such system on such date, or (C) the average of the bid and asked prices in the over-the-counter market at the close of trading on

such date if the shares are not traded on an Exchange or listed on the NASDAQ National Market System, or (D) if the security is not traded on an Exchange or in the over-the-counter market, the fair market value of a share of Common Stock on such date as determined in good faith by the Board of Directors. If the holder disagrees with the determination of the Market Value of any securities of the Common Stock determined by the Board of Directors under Section 1(d)(i)(D) the Market Value shall be determined by an independent appraiser acceptable to the Company and the holder. If they cannot agree on such an appraiser, then each of the Company and the holder shall select an independent appraiser, such two appraisers shall select a third independent appraiser and Market Value shall be the median of the appraisals made by such appraisers). If there is one appraiser, the cost of the appraisal shall be shared equally between the Company and the holder. If there are three appraisers, each of the Company and the holder shall pay for its own appraiser and shall share equally the cost of the third appraiser.

(e) Notwithstanding anything to the contrary contained herein, and in accordance with Section 713 of the American Stock Exchange Company Guide, in no event shall this Warrant to be exercisable for, and the Company shall have no obligation to issue, an amount exceeding 68,704 shares of the Company's Common Stock until such time the Company's shareholders shall have approved the issuance of shares in an amount exceeding 19.9% of the Company's outstanding Common Stock (determined as of the date hereof) at a price less than the current fair market value of the Common Stock upon the conversion of the Debentures and the exercise of the Warrants ("Shareholder Approval"). Immediately upon receipt of Shareholder Approval, this Warrant shall be exercisable in whole or in part in accordance with the provisions of Section 1 hereof. In accordance with the provisions of Section 9.12 of the Purchase Agreement, the Company covenants to seek Shareholder Approval as provided herein in this Section 1(e).

2. Transfer or Assignment of Warrant.

(a) Any assignment or transfer of this Warrant shall be made by surrender of this Warrant at the offices of the Company or at such other address as the Company may designate in writing to the registered holder hereof with the Assignment Form annexed hereto duly executed and accompanied by payment of any requisite transfer taxes, and the Company shall, without charge, execute and deliver a new Warrant of like tenor in the name of the assignee for the portion so assigned in case of only a partial assignment, with a new Warrant of like tenor to the assignor for the balance of the Warrant Shares purchasable.

(b) Prior to any assignment or transfer of this Warrant, the holder thereof shall deliver an opinion of counsel to the Company to the effect that the proposed transfer may be effected without registration under the Securities Act of 1933, as amended (the "Securities Act"). Each Warrant issued upon or in connection with such transfer shall bear the restrictive legend set forth on the front of this Warrant unless, in the opinion of the Company's counsel, such legend is no longer required to insure compliance with the Securities Act.

3. Adjustments to Warrant Price and Warrant Shares -- Anti-Dilution Provisions. In order to prevent dilution of the exercise right granted hereunder, the Warrant Price shall be subject to adjustment from time to time in accordance with this Section 3. Upon each adjustment of the Warrant Price pursuant to this Section 3, the holder shall thereafter be entitled

to acquire upon exercise of this Warrant, at the Applicable Warrant Price (as hereinafter defined), the number of shares of Common Stock obtainable by multiplying the Warrant Price in effect immediately prior to such adjustment by the number of shares of Common Stock acquirable immediately prior to such adjustment and dividing the product thereof by the Applicable Warrant Price resulting from such adjustment.

The Warrant Price in effect at the time of the exercise of this Warrant shall be subject to adjustment from time to time as follows:

(a) In the event that the Company shall at any time: (i) declare or pay to the holders of the Common Stock a dividend payable in any kind of shares of capital stock of the Company; or (ii) change or divide or otherwise reclassify its Common Stock into the same or a different number of shares with or without par value, or in shares of any class or classes; or (iii) transfer its property as an entirety or substantially as an entirety to any other company or entity; or (iv) make any distribution of its assets to holders of its Common Stock as a liquidation or partial liquidation dividend or by way of return of capital; then, upon the subsequent exercise of this Warrant, the holder thereof shall receive, in addition to or in substitution for the shares of Common Stock to which it would otherwise be entitled upon such exercise, such additional shares of stock or scrip of the Company, or such reclassified shares of stock of the Company, or such shares of the securities or property of the company resulting from transfer, or such assets of the Company, which it would have been entitled to receive had it exercised these rights prior to the happening of any of the foregoing events. If, at any time during the Exercise Period, the number of outstanding shares of Common Stock is (i) increased by a stock dividend payable in shares of Common Stock or by a subdivision or split up of shares of Common Stock, or (ii) decreased by a combination of shares of Common Stock, then, simultaneously with the occurrence of such event, the Warrant Price shall be adjusted automatically to a new amount equal to the product of (A) the Warrant Price in effect on such record date and (B) the quotient obtained by dividing (x) the number of shares of Common Stock outstanding on such record date (without giving effect to the events referred to in the foregoing clauses (i) or (ii)) by (y) the number of shares of Common Stock which would be outstanding immediately after the event referred to in the foregoing clauses (i) or (ii).

(b) If at any time after the date of issuance hereof the Company shall grant or issue any shares of Common Stock, or grant or issue any rights or options for the purchase of, or stock or other securities convertible into, Common Stock (such convertible stock or securities being herein collectively referred to as "Convertible Securities") other than:

(i) shares issued in a transaction described in subsection 3(c); or

(ii) shares issued, subdivided or combined in transactions described in subsection 3(a) if and to the extent that the number of shares of Common Stock receivable upon exercise of this Warrant shall have been previously adjusted pursuant to subsection 3(a) as a result of such issuance, subdivision or combination of such securities;

for a consideration per share which is less than the Fair Market Value (as hereinafter defined) of the Common Stock, then the Warrant Price in effect immediately prior to such issuance or sale (the "Applicable Warrant Price") shall, and thereafter upon each issuance or sale for a

consideration per share which is less than the Fair Market Value of the Common Stock, the Applicable Warrant Price shall, simultaneously with such issuance or sale, be adjusted, so that such Applicable Warrant Price shall equal a price determined by multiplying the Applicable Warrant Price by a fraction, the numerator of which shall be:

(A) the sum of (x) the total number of shares of Common Stock outstanding when the Applicable Warrant Price became effective, plus (y) the number of shares of Common Stock which the aggregate consideration received, as determined in accordance with subsection 3(d) for the issuance or sale of such additional Common Stock or Convertible Securities deemed to be an issuance of Common Stock as provided in subsection 3(e), would purchase (including any consideration received by the Company upon the issuance of any shares of Common Stock since the date the Applicable Warrant Price became effective not previously included in any computation resulting in an adjustment pursuant to this subsection 3(b)) at the Fair Market Value of the Common Stock; and the denominator of which shall be

(B) the total number of shares of Common Stock outstanding (or deemed to be outstanding as provided in subsection 3(e) hereof) immediately after the issuance or sale of such additional shares.

For purposes of this Section 3, "Fair Market Value" shall mean the average of the closing price of the Common Stock for each of the twenty (20) consecutive trading days prior to such issuance or sale on an Exchange or if shares of Common Stock are not listed on an Exchange during such period, the closing price per share as reported by NASDAQ National Market System if the shares are quoted on such system during such period, or the average of the bid and asked prices of the Common Stock in the over-the-counter market at the close of trading during such period if the shares are not traded on an Exchange or listed on the NASDAQ National Market System, or if the Common Stock is not traded on an Exchange or in the over-the-counter market, the fair market value of a share of Common Stock during such period as determined in good faith by the Board of Directors.

If, however, the Applicable Warrant Price thus obtained would result in the issuance of a lesser number of shares upon conversion than would be issued at the initial Warrant Price, the Applicable Warrant Price shall be such initial Warrant Price.

Upon each adjustment of the Warrant Price pursuant to this subsection 3(b), the total number of shares of Common Stock for which this Warrant shall be exercisable shall be such number of shares (calculated to the nearest tenth) purchasable at the Applicable Warrant Price multiplied by a fraction, the numerator of which shall be the Warrant Price in effect immediately prior to such adjustment and the denominator of which shall be the exercise price in effect immediately after such adjustment.

(c) Anything in this Section 3 to the contrary notwithstanding, no adjustment in the Warrant Price shall be made in connection with:

(i) the grant, issuance or exercise of any Convertible Securities pursuant to the Company's qualified or non-qualified Employee Stock Option Plans or any other bona fide employee benefit plan or incentive arrangement, adopted or approved by the Company's Board of Directors or approved by the Company's shareholders, as may be amended from time to time, or under any other bona fide employee benefit plan hereafter adopted by the Company's Board of Directors; or

(ii) the grant, issuance or exercise of any Convertible Securities in connection with the hire or retention of any officer, director or key employee of the Company, provided such grant is approved by the Company's Board of Directors; or

(iii) the issuance of any shares of Common Stock pursuant to the grant or exercise of Convertible Securities outstanding as of the date hereof (exclusive of any subsequent amendments thereto).

(d) For the purpose of subsection 3(b), the following provisions shall also be applied:

(i) In case of the issuance or sale of additional shares of Common Stock for cash, the consideration received by the Company therefor shall be deemed to be the amount of cash received by the Company for such shares, before deducting therefrom any commissions, compensation or other expenses paid or incurred by the Company for any underwriting of, or otherwise in connection with, the issuance or sale of such shares.

(ii) In the case of the issuance of Convertible Securities, the consideration received by the Company therefor shall be deemed to be the amount of cash, if any, received by the Company for the issuance of such rights or options, plus the minimum amounts of cash and fair value of other consideration, if any, payable to the Company upon the exercise of such rights or options or payable to the Company upon conversion of such Convertible Securities.

(iii) In the case of the issuance of shares of Common Stock or Convertible Securities for a consideration in whole or in part, other than cash, the consideration other than cash shall be deemed to be the fair market value thereof as reasonably determined in good faith by the Board of Directors of the Company (irrespective of accounting treatment thereof); provided, however, that if such consideration consists of the cancellation of debt issued by the Company, the consideration shall be deemed to be the amount the Company received upon issuance of such debt (gross proceeds) plus accrued interest and, in the case of original issue discount or zero coupon indebtedness, accrued value to the date of such cancellation, but not including any premium or discount at which the debt may then be trading or which might otherwise be appropriate for such class of debt.

(iv) In case of the issuance of additional shares of Common Stock upon the conversion or exchange of any obligations (other than Convertible Securities), the amount of the consideration received by the Company for such Common Stock

shall be deemed to be the consideration received by the Company for such obligations or shares so converted or exchanged, before deducting from such consideration so received by the Company any expenses or commissions or compensation incurred or paid by the Company for any underwriting of, or otherwise in connection with, the issuance or sale of such obligations or shares, plus any consideration received by the Company in connection with such conversion or exchange other than a payment in adjustment of interest and dividends. If obligations or shares of the same class or series of a class as the obligations or shares so converted or exchanged have been originally issued for different amounts of consideration, then the amount of consideration received by the Company upon the original issuance of each of the obligations or shares so converted or exchange shall be deemed to be the average amount of the consideration received by the Company upon the original issuance of all such obligations or shares. The amount of consideration received by the Company upon the original issuance of the obligations or shares so converted or exchanged and the amount of the consideration, if any, other than such obligations or shares, received by the Company upon such conversion or exchange shall be determined in the same manner as provided in paragraphs (i) and (ii) above with respect to the consideration received by the Company in case of the issuance of additional shares of Common Stock or Convertible Securities.

(v) In the case of the issuance of additional shares of Common Stock as a dividend, the aggregate number of shares of Common Stock issued in payment of such dividend shall be deemed to have been issued at the close of business on the record date fixed for the determination of stockholders entitled to such dividend and shall be deemed to have been issued without consideration; provided, however, that if the Company, after fixing such record date, shall legally abandon its plan to so issue Common Stock as a dividend, no adjustment of the Applicable Conversion Price shall be required by reason of the fixing of such record date.

(e) For purposes of the adjustment provided for in subsection 3(b) above, if at any time the Company shall issue any Convertible Securities, the Company shall be deemed to have issued at the time of the issuance of such Convertible Securities the maximum number of shares of Common Stock issuable upon conversion of the total amount of such Convertible Securities.

(f) On the expiration, cancellation or redemption of any Convertible Securities, the Warrant Price then in effect hereunder shall forthwith be readjusted to such Warrant Price as would have been obtained (a) had the adjustments made upon the issuance or sale of such expired, canceled or redeemed Convertible Securities been made upon the basis of the issuance of only the number of shares of Common Stock theretofore actually delivered upon the exercise or conversion of such Convertible Securities (and the total consideration received therefor) and (b) had all subsequent adjustments been made on only the basis of the Warrant Price as readjusted under this subsection 3(f) for all transactions (which would have affected such adjusted Warrant Price) made after the issuance or sale of such Convertible Securities.

(g) Anything in this Section 3 to the contrary notwithstanding, no adjustment in the Warrant Price shall be required unless such adjustment would require an increase or decrease of at least 1% in such Warrant Price; provided, however, that any adjustments which by

reason of this subsection 3(g) are not required to be made shall be carried forward and taken into account in making subsequent adjustments. All calculations under this Section 3 shall be made to the nearest cent.

(h) If, at any time while this Warrant is outstanding, the Company shall pay any dividend payable in cash or in Common Stock, shall offer to the holders of its Common Stock for subscription or purchase by them any shares of stock of any class or any other rights, shall enter into an agreement to merge or consolidate with another corporation, shall propose any capital reorganization or reclassification of the capital stock of the Company, including any subdivision or combination of its outstanding shares of Common Stock or there shall be contemplated a voluntary or involuntary dissolution, liquidation or winding up of the Company, the Company shall cause notice thereof to be mailed to the registered holder of this Warrant at its address appearing on the registration books of the Company, at least thirty (30) days prior to the record date as of which holders of Common Stock shall participate in such dividend, distribution or subscription or other rights or at least thirty (30) days prior to the effective date of the merger, consolidation, reorganization, reclassification or dissolution. Upon any adjustment of any Warrant Price, then and in each such case the Company shall promptly deliver a notice to the registered holder of this Warrant, which notice shall state the Warrant Price resulting from such adjustment, setting forth in reasonable detail the method of calculation and the facts upon which such calculation is based.

(i) If the Company is a party to a merger or other transaction which reclassifies or changes its outstanding Common Stock, upon consummation of such transaction this Warrant shall automatically become exercisable for the kind and amount of securities, cash or other assets which the holder of this Warrant would have owned immediately after such transaction if the holder had converted this Warrant at the Warrant Price in effect immediately before the effective date of the transaction. Concurrently with the consummation of such transaction, the person obligated to issue securities or deliver cash or other assets upon exercise of this Warrant shall execute and deliver to the holder a supplemental Warrant so providing and further providing for adjustments which shall be as nearly equivalent as may be practical to the adjustments provided in this Section 3. The successor company shall mail to the holder a notice describing the supplemental Warrant.

If securities deliverable upon exercise of this Warrant, as provided above, are themselves convertible into or exercisable for the securities of an affiliate of a corporation formed, surviving or otherwise affected by the merger or other transaction, that issuer shall join in the supplemental Warrant which shall so provide. If this subsection 3(i) applies, subsection 3(a) does not apply.

4. Charges, Taxes and Expenses. The issuance of certificates for Warrant Shares upon any exercise of this Warrant shall be made without charge to the holder of this Warrant for any tax or other expense in respect to the issuance of such certificates, all of which taxes and expenses shall be paid by the Company, and such certificates shall be issued only in the name of the holder of this Warrant.

5. Miscellaneous.

(a) The terms of this Warrant shall be binding upon and shall inure to the benefit of any successors or assigns of the Company and of the holder or holders hereof and

of the shares of Common Stock issued or issuable upon the exercise hereof.

(b) No holder of this Warrant, as such, shall be entitled to vote or receive dividends or be deemed to be a stockholder of the Company for any purpose, nor shall anything contained in this Warrant be construed to confer upon the holder of this Warrant, as such, any rights of a stockholder of the Company or any right to vote, give or withhold consent to any corporate action, receive notice of meetings, receive dividends or subscription rights, or otherwise.

(c) Receipt of this Warrant by the holder hereof shall constitute acceptance of an agreement to the foregoing terms and conditions.

(d) The Warrant and the performance of the parties hereunder shall be construed and interpreted in accordance with the laws of the State of New York without giving effect to its conflict of laws rules wherein it was negotiated and executed and the parties hereunder consent and agree that the State and Federal Courts which sit in the State of New York and the County of New York shall have exclusive jurisdiction with respect to all controversies and disputes arising hereunder.

(e) This Warrant is subject to certain provisions contained in the Debenture and Warrant Purchase Agreement dated May 26, 1999 among the Company and various other parties, (including, without limitation, the registration rights provisions of Article XI thereof) copies of which are on file with the Secretary of the Company. Shares issued upon exercise of this Warrant shall contain a legend substantially to the same effect as the legend set forth on the first page of this Warrant.

IN WITNESS WHEREOF, the Company has caused this Warrant to be signed by its duly authorized officer and its corporate seal to be affixed hereto.

Dated as of May 26, 1999

HALSEY DRUG CO., INC.

BY:

Name: Michael Reicher
Title: President

SUBSCRIPTION FORM

(TO BE EXECUTED BY THE REGISTERED HOLDER
IF HE DESIRES TO EXERCISE THE WARRANT)

TO: HALSEY DRUG CO., INC.

The undersigned hereby exercises the right to purchase _____ shares of Common Stock, par value $.01 per share, covered by the attached Warrant in accordance with the terms and conditions thereof, and herewith makes payment of the Warrant Price for such shares in full.

SIGNATURE

ADDRESS

DATED:_____

NOTICE OF EXERCISE OF COMMON STOCK WARRANT
PURSUANT TO NET ISSUE ("CASHLESS") EXERCISE PROVISIONS

[Date]

- ---

Halsey Drug Co., Inc.
a New York corporation
695 N. Perryville Road
Rockford, Illinois 61107
Attention:_____

Aggregate Price of $
of Warrant
Aggregate Price
Being
Exercised: $

Warrant Price
(per share): $

Market Value
(per share): $

Number of Shares
of Common Stock
under this
Warrant:

Number of Shares
of Common Stock
to be Issued
Under this
Notice:

CASHLESS EXERCISE

Gentlemen:

The undersigned, the registered holder of the Warrant to Purchase Common Stock delivered herewith ("Warrant"), hereby irrevocably exercises such Warrant for, and purchases thereunder, shares of the Common Stock of HALSEY DRUG CO., INC., a New York corporation, as provided below. Capitalized terms used herein, unless otherwise defined herein, shall have the meanings given in the Warrant. The portion of the Aggregate Price (as hereinafter defined) to be applied toward the purchase of Common Stock pursuant to this Notice of Exercise is $, thereby leaving a remainder Aggregate Price (if any) equal to $. Such exercise shall be pursuant to the net issue exercise provisions of Section 1(b) of the Warrant; therefore, the holder makes no payment with this Notice of Exercise. The number of shares to be issued pursuant to this exercise shall be determined by reference to the formula in Section 1(b) of the Warrant which requires the use of the Market Value (as defined in Section 1(d) of the Warrant) of the Company's Common Stock on the business day immediately preceding the day on which this Notice is received by the Company. To the extent the foregoing exercise is for less than the full Aggregate Price of the Warrant, the remainder of the Warrant representing a number

of Shares equal to the quotient obtained by dividing the remainder of the Aggregate Price by the Warrant Price (and otherwise of like form, tenor and effect) may be exercised under Section 1(a) of the Warrant. For purposes of this Notice the term "Aggregate Price" means the product obtained by multiplying the number of shares of Common Stock for which the Warrant is exercisable times the Warrant Price.

SIGNATURE

Date:_____
Address

ASSIGNMENT

(TO BE EXECUTED BY THE REGISTERED HOLDER
IF HE DESIRES TO TRANSFER THE WARRANT)

FOR VALUE RECEIVED, the undersigned hereby sells, assigns and transfers unto the right to purchase shares of Common Stock of HALSEY DRUG CO., INC., evidenced by the within Warrant, and does hereby irrevocably constitute and appoint _____ Attorney to transfer the said Warrant on the books of the Company, with full power of substitution.

Signature

Address

Dated:_____

In the Presence of:

_____

Exhibit 10.75

LEASE TERMINATION AND SETTLEMENT AGREEMENT

THIS LEASE TERMINATION AND SETTLEMENT AGREEMENT (this "Agreement") is made as of March 21, 2000, by and between MILTON J. ACKERMAN, SUE ACKERMAN, LEE HINDERSTEIN, THELMA HINDERSTEIN and MARILYN WEISS, individuals doing business as MILTON J. ACKERMAN, ET AL. and ATLANTIC PROPERTY COMPANIES, each a [New York] general partnership (collectively "Landlord"), and HALSEY DRUG CO., INC., a New York corporation ("Tenant").

W I T N E S S E T H :

WHEREAS, Landlord and Tenant are parties to certain agreements described on Exhibit A annexed hereto (which agreements are hereinafter collectively referred to as the "Lease"), pursuant to which Landlord leased to Tenant and tenant occupied certain premises located in Brooklyn, New York, as further described in the Lease (the "Premises"); and

WHEREAS, Landlord and Tenant have agreed to terminate the Lease and settle all disputes, claims and obligations between Landlord and Tenant, and Tenant has agreed to surrender the Premises, all upon the terms and conditions contained in this Agreement;

NOW, THEREFORE, for good and valuable consideration, the receipt and legal sufficiency of which is hereby acknowledged by each of the parties hereto, Landlord and Tenant agree as follows:

1. Simultaneous with the execution of this Agreement, Tenant has paid to Landlord the sum of $215,860.00, representing all rent and other charges payable by Tenant to Landlord under the Lease through and including March 31, 2000, receipt of which is hereby acknowledged by Landlord.

2. Tenant has advised Landlord that Tenant is currently negotiating a transaction with an unrelated third party which, among other things, would provide funds sufficient for Tenant to satisfy its obligations under this Agreement (the "Third Party Transaction"). Landlord understands that there is no assurance that Tenant will consummate a Third Party Transaction acceptable to it on or before April 18, 2000. Tenant may rescind its obligations under this Agreement by delivering written notice to that effect to Landlord at any time after April 18, 2000, if it shall not have consummated a Third Party Transaction acceptable to it in its sole discretion on or before the date on which Tenant delivers its termination notice to Landlord. Landlord may rescind its obligations under this Agreement by delivering to Tenant written notice to that effect at any time after April 18, 2000 if Tenant shall not have paid the amounts specified in Paragraph 3 below on or before April 18, 2000.

3. On the earlier to occur of April 18, 2000 and the second business day immediately following the closing and funding of the Third Party Transaction, Tenant shall pay the following amounts in immediately available funds by wire transfer:

(a) To Landlord, in accordance with the wire transfer

instructions set forth on Exhibit B, the sum of $488,250.00, representing the fair value for the use and occupancy of the Premises by Tenant for the period April 1, 2000 through and including August 31, 2000, in lieu of any and all rent and other amounts payable by Tenant under the Lease.

(b) To Landlord, in accordance with the wire transfer instructions set forth on Exhibit B, the sum of $1,150,000.00 in consideration of the termination of the Lease prior to its stated expiration date and the agreements of the parties contained in this Agreement.

(c) To St. John & Wayne, L.L.C. ("Tenant's Counsel"), in accordance with the wire transfer instructions set forth on Exhibit C annexed hereto, the sum of $390,600.00, which amount shall (i) constitute the "Liquidated Amount" described in Paragraph 5, and (ii) be held in escrow by Tenant's Counsel in accordance with the provisions of Paragraph 5 of this Agreement.

(d) To Graubard, Mollen & Miller ("Landlord's Counsel"), in accordance with the wire transfer instructions set forth on Exhibit D annexed hereto, the sum of $200,000.00(provided, however, Landlord acknowledges that it is currently holding as a security deposit under the Lease the sum of $81,373 which amount shall be credited against Tenant's payment obligation under this Paragraph 3(d), leaving a balance payable by Tenant under this Paragraph 3(d) of $118,627), which amount shall constitute the (i) "Restoration Amount" described in Paragraph 6, and (ii) be held in escrow by Landlord's Counsel in accordance with the provisions of Paragraph 6 of this Agreement.

4. The term of the Lease shall expire and the obligations of Landlord and Tenant under the Lease shall terminate at 11:59 p.m. on the date (the "Termination Date") which is the later to occur of (a) August 31, 2000 and (b) the Surrender Date (hereinafter defined). The "Surrender Date" shall be the date on which Tenant has (i) removed its trade fixtures, equipment and other personal property of Tenant located in the Premises, except for those items described on Schedule H hereto (ii) provided notice to Landlord that Tenant has ceased all business operations at and vacated the Premises, and (iii) delivered to the Landlord all keys to the Premises in its possession. Time is of the essence for the Surrender Date to occur on or before March 31, 2001. Simultaneous with the execution of this Agreement, Tenant has executed and delivered to the Landlord's Counsel a written Stipulation consenting to the entry of a final judgment of possession with respect to the Premises and a warrant of eviction in the form of Exhibit G annexed hereto, which shall be held in escrow by Landlord's Counsel and shall not be released from escrow and presented to the court for entry until after March 31, 2001 as long as Tenant complies with the provisions of Paragraph 3 hereof. If Tenant fails to comply with the provisions of Paragraph 3 and Landlord or Tenant has rescinded its obligations under this Agreement in accordance with Paragraph 2 hereof, the Stipulation, this Agreement and the other documents needed to implement this Agreement shall be null and void and of no force or effect.

5. (a) If the Surrender Date shall occur on or (i) after September 1, 2000, Landlord shall be entitled to receive the Liquidated Amount and all interest earned thereon, or (ii) before August 31, 2000, Tenant shall be entitled to receive the Liquidated Amount and all interest earned thereon. The parties agree that the Liquidated Amount represents the (i) consideration for Landlord's granting to Tenant the right to remain in possession of the Premises after August 31, 2000, and (ii) fair value for the use and occupancy of the Premises by Tenant for any period of time from and after September 1, 2000 through and including the Surrender Date, in lieu of any and all rent or other charges payable by Tenant under the Lease.

(b) The Liquidated Amount shall be deposited in an interest bearing attorney trust account by Tenant's Counsel, which account shall be reasonably acceptable to Landlord and Tenant.

(c) If Landlord shall claim that the Surrender Date occurred on or after September 1, 2000, it shall provide written notice thereof to Tenant, with a copy to Tenant's Counsel and Landlord's Counsel, specifying in reasonable detail the facts on which such claim is based. In the event that Tenant does not dispute such claim within three (3) business days after receipt of Landlord's notice, Tenant's Counsel shall on the fourth (4th) business day after receipt of Landlord's notice promptly deliver to Landlord the Liquidated Amount and all interest earned thereon. In the event, however, that Tenant shall elect to dispute such claim, it shall be required, within three (3) business days after receipt of Landlord's notice hereunder, to provide written notice thereof to Landlord, with a copy to Tenant's Counsel and Landlord's Counsel, specifying in reasonable detail the facts on which any such dispute is based. In the event of any such dispute, Landlord and Tenant agree that such dispute shall be settled by arbitration in accordance with the provisions of Paragraph 7 of this Agreement. Tenant's Counsel shall retain the Liquidated Amount until its receipt of a certified copy of any such final and non-appealable arbitration decision or award or joint written notice from Landlord and Tenant stating the dispute has been settled and specifying the manner in which the Liquidated Amount is to be disbursed, at which time it shall promptly deliver to Landlord or Tenant, as the case may be, the Liquidated Amount and all interest earned thereon.

(d) If Tenant shall claim that the Surrender Date occurred on or before August 31, 2000, it shall provide written notice thereof to Landlord, with a copy to Tenant's Counsel and Landlord's Counsel. In the event that Landlord does not dispute such claim within three (3) business days after receipt of Tenant's notice, Tenant's Counsel shall on the fourth (4th) day after receipt of Tenant's notice promptly deliver to Tenant the Liquidated Amount and all interest earned thereon. In the event, however, that Landlord shall dispute such claim it shall be required, within three (3) business days after receipt of Tenant's notice, to provide written notice thereof to Tenant, with a copy to Tenant's Counsel and Landlord's Counsel, specifying in reasonable detail the facts on which any such dispute is based. In the event of any such dispute, Landlord and Tenant agree that such dispute shall be settled by final and non-appealable arbitration in accordance with the provisions of Paragraph 7 of this Agreement. Tenant's Counsel shall retain the Liquidated Amount until its receipt of a certified copy of any such arbitration decision or award or joint written notice from Landlord and Tenant stating the dispute has been settled and specifying the manner in which the Liquidated Amount is to be disbursed, at which time it shall promptly deliver to Landlord or Tenant, as the case may be, the Liquidated Amount and all

interest earned thereon.

(e) Landlord and Tenant agree that Tenant's Counsel shall not be liable for any error or judgment or for any mistake of fact, law for anything which it may do or refrain from doing in connection herewith, except its own gross negligence or willful misconduct. Landlord and Tenant agree to indemnify, hold harmless and defend Tenant's Counsel from any loss, damage, claim, liability, judgment, expense (including attorney's fees and disbursements) or other charge incurred or sustained by it by reason of any act or omission performed or omitted hereunder, but this indemnity shall not be applicable to any loss, liability, damage, claim, judgment, expense or other charge resulting from the gross negligence or willful misconduct of Tenant's Counsel. Tenant's Counsel shall have the right to rely conclusively upon the notices delivered hereunder, and shall be under no obligation to ascertain the authenticity of such notices, nor to determine the factual accuracy thereof. Tenant's Counsel is acting as a stakeholder only with respect to the Liquidated Amount. If there is any dispute as to whether Tenant's Counsel is obligated to deliver the Liquidated Amount and/or to whom it should be delivered, Tenant's Counsel shall not make any delivery, but in such event Tenant's Counsel shall hold the Liquidated Amount until receipt by Tenant's Counsel of an authorization in writing signed by all parties having an interest in such dispute directing the disposition of same, or in the absence of such authorization Tenant's Counsel shall hold the Liquidated Amount until the final determination of the rights of the parties in an appropriate proceeding. If such written authorization is not given, or proceedings for such determination are not begun within a reasonable period of time and diligently continued, Tenant's Counsel shall have the right, at any time thereafter, to commence an action or proceeding, at the sole cost of expense of Landlord and Tenant, in the nature of interpleader in any court having jurisdiction thereof, and to deposit the Liquidated Amount with such court, and thereupon be discharged from any and all further liability hereunder. Landlord acknowledges that Tenant's Counsel is a law firm which represents Tenant and Tenant's Counsel shall be entitled to represent Tenant in any and all matters arising, directly or indirectly, out of the Lease and this Agreement and the transactions contemplated hereby, including, without limitation, the disposition of the Liquidated Amount. Landlord waives any conflicts of interest or appearance of impropriety, if any, that may be occasioned by Tenant's Counsel's role as a stakeholder, witness or party in any proceedings involving the parties. Notwithstanding anything in this Paragraph 5(e) to the contrary, Landlord shall not be liable to Tenant's Counsel for the payment of any attorneys' fees or disbursements which are attributable to Tenant's Counsel's representation of Tenant.

6. (a) The Restoration Amount shall be deposited in an interest bearing trust account by Landlord's Counsel, which account shall be reasonably acceptable to Landlord and Tenant.

(b) On the Surrender Date, Tenant shall surrender the Premises to Landlord in its then "as is" condition, and, notwithstanding anything to the contrary contained in the Lease, except to the extent as specifically provided in Paragraph 6(c) of this Agreement, Tenant shall not be required to perform any maintenance, repair, alteration, improvement, replacement or restoration to the Premises. In consideration of any maintenance, repair, alteration, improvement, restoration or removal obligation of Tenant under the Lease and any unpaid water, sewer or utility charges allocable to the Premises through and including the Surrender Date for which Tenant was obligated under the Lease, including, without limitation, under Articles 3, 4, 22 and 29 of the Lease (collectively, the "Tenant Obligations"), Tenant has deposited the Restoration

Amount. The parties agree that the Restoration Amount shall be payable to Landlord if and to the extent that Landlord, on or before the period expiring one hundred and fifty (150) days after the Surrender Date (the "Outside Date"), shall incur any costs in respect of the Tenant Obligations. The parties agree that the Tenant shall have no liability in respect of any or all of the Tenant Obligations other than the Restoration Amount as provided in Paragraph 3(d) above and Landlord's recovery of any amounts claims, damages, fees, costs or for such Tenant Obligations are expressly limited to the Restoration Amount.

(c) Notwithstanding the foregoing, prior to the Surrender Date (i) Tenant shall perform normal and customary maintenance and repair services and pay all water, sewer and utility bills relating to the Premises; provided, however, that Tenant shall not be obligated to maintain, repair or replace any part or portion of the Premises, including, without limitation, the HVAC systems, where the cost of such maintenance or repair shall exceed $25,000, in the aggregate for all such maintenance, repair or replacement items (based on a good faith estimate received by Tenant), and (ii) Tenant shall exercise reasonable care in the removal of its equipment, fixtures and other personal property from the Premises. Each of the Tenant and the Landlord hereby acknowledge and agree that any breach by Tenant of the terms and provisions of this Paragraph 6(c) shall not be deemed to constitute or otherwise result in a default or breach by Tenant of this Agreement or the Lease and Landlord's sole remedy for a breach by Tenant of its obligations under this Paragraph 6(c) shall be a claim against the Restoration Amount and any insurance maintained by Tenant for the Premises where the Landlord is named as an insured under such insurance.

(d) Within thirty (30) days after the Outside Date, Landlord shall provide notice to Tenant, with a copy to Landlord's Counsel and Tenant's Counsel, describing in reasonable detail the work performed and the costs incurred by Landlord on or before the Outside Date in respect of Tenant Obligations for which Landlord claims it is entitled to reimbursement under Paragraph 6(b) (the "Restoration Claim"). If Tenant does not dispute the Restoration Claim in whole or in part, within ten (10) days after receipt by Landlord's Counsel of the Restoration Claim notice, Landlord's Counsel shall on the eleventh (11th) day after receipt of such notice promptly deliver to Landlord such portion of the Restoration Amount equal to the amount of the Restoration Claim. In the event, however, that Tenant shall elect to dispute the Restoration Claim, in whole or in part, it shall be required, within ten (10) days after receipt of the Restoration Claim notice from Landlord, to provide notice thereof to Landlord, with a copy to Landlord's Counsel and Tenant's Counsel. In the event of any such dispute or contest, Landlord and Tenant hereby agree that any such dispute shall be settled by arbitration in accordance with the provisions of Paragraph 7 of this Agreement. Landlord's Counsel shall disburse the portion, if any, of the Restoration Amount equal to any Restoration Claim which is not disputed by Tenant and shall retain the portion of the Restoration Amount covered by any such dispute until its receipt of a certified copy of any final and non-appealable arbitration decision or award or joint written notice from Landlord and Tenant stating the dispute has been settled and specifying the manner in which the Restoration Amount is to be disbursed, at which time it shall promptly deliver to the appropriate party or parties a check or checks in the amount of any such judgment or award.

(e) On the date which is thirty (30) days after the Outside Date, Landlord's Counsel shall deliver to Tenant the balance of the Restoration Amount (plus accrued interest),

reduced by any amounts due to Landlord pursuant to the terms of this Paragraph 6 and any amounts which are the subject of an Unresolved Claim. The term "Unresolved Claim" shall mean any claim which may be made against the Restoration Amount in accordance with this Paragraph 6, until such time as such claim has been paid in full or otherwise fully settled, compromised or adjusted by the parties and Landlord's Counsel, and the amount of any such Unresolved Claim shall remain with Landlord's Counsel until so settled or adjusted and then paid to the party to whom such funds are to be paid pursuant to such agreement, settlement, compromise or adjustment.

(f) Landlord and Tenant agree that Landlord's Counsel shall not be liable for any error or judgment or for any mistake of fact, law for anything which it may do or refrain from doing in connection herewith, except its own gross negligence or willful misconduct. Landlord and Tenant agree to indemnify, hold harmless and defend Landlord's Counsel from any loss, damage, claim, liability, judgment, expense (including attorney's fees and disbursements) or other charge incurred or sustained by it by reason of any act or omission performed or omitted hereunder, but this indemnity shall not be applicable to any loss, liability, damage, claim, judgment, expense or other charge resulting from the gross negligence or willful misconduct of Landlord's Counsel. Landlord's Counsel shall have the right to rely conclusively upon the notices delivered hereunder, and shall be under no obligation to ascertain the authenticity of such notices, nor to determine the factual accuracy thereof. Landlord's Counsel is acting as a stakeholder only with respect to the Restoration Amount. If there is any dispute as to whether Landlord's Counsel is obligated to deliver the Restoration Amount and/or to whom it should be delivered, Landlord's Counsel shall not make any delivery, but in such event Landlord's Counsel shall hold the Restoration Amount until receipt by Landlord's Counsel of an authorization in writing signed by all parties having an interest in such dispute directing the disposition of same, or in the absence of such authorization Landlord's Counsel shall hold the Restoration Amount until the final determination of the rights of the parties in an appropriate proceeding. If such written authorization is not given, or proceedings for such determination are not begun within a reasonable period of time and diligently continued, Landlord's Counsel shall have the right, at any time thereafter, to commence an action or proceeding, at the sole cost of expense of Landlord and Tenant, in the nature of interpleader in any court having jurisdiction thereof, and to deposit the Restoration Amount with such court, and thereupon be discharged from any and all further liability hereunder. Tenant acknowledges that Landlord's Counsel is a law firm which represents Landlord and Landlord's Counsel shall be entitled to represent Landlord in any and all matters arising, directly or indirectly, out of the Lease and this Agreement and the transactions contemplated hereby, including, without limitation, the disposition of the Restoration Amount. Tenant waives all conflicts of interest or appearance of impropriety, if any, that may be occasioned by Landlord's Counsel's role as stakeholder, witness or party in any proceedings involving the parties. Notwithstanding anything in this Paragraph 6(f) to the contrary, Tenant shall not be liable to Landlord's Counsel for the payment of any attorneys' fees or disbursements which are attributable to Landlord's Counsel's representation of Landlord.

7. (a) In the event that any contest or dispute set forth in Paragraphs 5 or 6 of this Agreement is to be resolved by arbitration, the party invoking the arbitration procedure (the "First Party") shall give written notice (the "Arbitration Notice") to the other party (the "Second Party"), and shall in such Arbitration Notice appoint an arbitrator on its behalf. Within ten (10) days after its receipt of such Arbitration Notice, the Second Party by notice to the First Party

shall appoint an arbitrator on its behalf; and if the second arbitrator shall not be so appointed with such ten (10) days, the First Party shall appoint the second arbitrator. The two arbitrators appointed pursuant to the above shall try to appoint a third independent arbitrator. If, within fourteen (14) days after the appointment of the second arbitrator they have not agreed upon the appointment of a third independent arbitrator, then either party may apply to the American Arbitration Association ("AAA") for the appointment of such third independent arbitrator and the other party shall not raise any questions as to the AAA's full power and jurisdiction to entertain the application and make the appointment. Each arbitrator shall have at least ten (10) years' experience in a calling pertaining to the type of matter in dispute. The date on which the third independent arbitrator is appointed is referred to as the "Appointment Date". Discovery shall be permitted, including, without limitation, the production of documents, identification of witnesses and experts and depositions.

(b) As soon as practicable after the Appointment Date, the matter in dispute shall be arbitrated by the parties in accordance with the commercial rules then in force of the AAA; provided, however, that each party shall be entitled to discovery proceedings in accordance with the rules of New York Civil Practice Law and Rules, and the failure of any party to so submit to such discovery upon the request of the other shall provide the basis for termination of arbitration procedure and the filing of a law suit in the Supreme Court of the State of New York, County of Kings. The resolution of the dispute shall be determined by the majority of the three arbitrators, shall constitute an "award" within the meaning of the applicable rules of the AAA and applicable law, and judgment may be entered thereon in any court of competent jurisdiction.

(c) Landlord and Tenant hereby submit to the in personam jurisdiction of the AAA in the State of New York and agree that any process in any arbitration proceeding hereunder may be personally served upon Landlord or Tenant within or outside the State of New York. The arbitration shall be conducted at a location in New York City mutually acceptable to Landlord and Tenant.

(d) Each party shall pay its own fees and expenses relating to the arbitration (including, without limitation, the fees and expenses of its counsel, its arbitrator and any experts or witnesses retained by it). Each party shall pay one-half (1/2) of the fees and expenses of the third independent arbitrator and of the AAA.

8. Simultaneous with the payment by Tenant of the amounts described in Paragraph 3 of this Agreement, (a) Landlord shall execute and deliver to Tenant a release in the form of Exhibit E annexed hereto ("Landlord's Release"), and (b) Tenant shall execute and deliver to Landlord a release in the form of Exhibit F annexed hereto ("Tenant's Release").

9. Notwithstanding anything to the contrary contained herein or in the Tenant's Release, Landlord shall defend, hold harmless and indemnify Tenant from and against any and all third party claims, causes of actions, proceedings and demands based on, relating to, arising out of or in connection with the Premises (the "Claims"), except to the extent such Claims are in the nature of those expressly excluded from the Landlord's Release. Nothing contained herein or in the Landlord's Release is intended, and shall not be deemed, to constitute a waiver or modification by Tenant of, or Tenant's release of Landlord from, any claim for indemnification,

contribution or similar claims, rights, interests, remedies Tenant may possess against the Landlord relating to, arising from, pertaining to, directly or indirectly, any federal, state or local law, rule, ordinance or regulation governing environmental claims, conditions or obligations impacting or otherwise affecting the Premises.

10. Tenant shall maintain in effect through and including the Surrender Date such third-party insurance coverage as Tenant is required to maintain under the Lease. Tenant agrees that if such insurance does not afford coverage on an "occurrence" basis, Tenant shall, on or before the Surrender Date, purchase a "tail" policy, naming Landlord as an additional insured thereon, which "tail" policy shall provide coverage for claims made for a period of not less than three (3) years after the Surrender Date.

11. Landlord and Tenant warrant and represent to each other as follows:

(a) All consents or approvals required for the execution of this Agreement and the performance of the obligations of the parties hereunder, if any, have been obtained.

(b) The Lease, the Term Sheet dated March 16, 2000 and this Agreement, are the only agreements in existence with respect to the demise and lease of the Premises by Landlord to Tenant and the use and occupancy of the Premises by Tenant.

(c) Neither party has dealt with any real estate broker or similar agent in connection with the negotiation or execution of this Agreement.

(d) Each party has the full power and authority to enter into this Agreement and perform its obligations hereunder, subject to the provisions of this Agreement, and the individuals executing this Agreement on behalf of each party have the full power and authority to bind such party.

12. This Agreement and the covenants and conditions contained in this Agreement shall be binding upon and inure to the benefit of the parties hereto and their respective successors and assigns. This Agreement sets forth the entire agreement and understanding between the parties with respect to the subject matter of this Agreement and supersedes all other prior agreements and understandings of the parties. This Agreement may not be terminated, modified or otherwise changed, except pursuant to a written agreement signed by Landlord and Tenant.

13. All notices and other communications under this Agreement must be in writing and will be deemed to have been duly given when (a) delivered by hand (with written confirmation of receipt), (b) sent by telecopier (with written confirmation of receipt), provided that copy is mailed by certified mail, return receipt requested, or (c) received by the addressee, if sent by a nationally recognized overnight delivery service (receipt requested), 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 by notice to the other parties):

If to Landlord:

Marilyn Weiss
1100 Park Avenue

New York, New York 10028
Facsimile No.: (212) 534-4181

If to Landlord's Counsel:

Graubard, Mollen & Miller
600 Third Avenue
New York, New York 10016
Attention: Michael A. Salberg, Esq.
Facsimile No.: (212)818-8881

If to Tenant:

Halsey Drug Co., Inc.
695 Perryville Road
Crimson Bldg. 2
Rockford, Illinois 61107
Attention: Peter A. Clemens
Facsimile No.: (815)399-9710

If to Tenant's Counsel:

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

A copy of any notice given to Landlord shall also be given to Landlord's Counsel, and a copy of any notice given to Tenant shall also be given to Tenant's Counsel. Notice is given by an attorney for a party shall be deemed to be notice given by such party.

14. This Agreement shall be governed by and construed under the laws of the State of New York (except as provided in Paragraphs 5, 6 and 7 of this Agreement) and all disputes, law suits and other controversies shall be instituted exclusively in the courts of the State of New York.

15. Landlord warrants and represents to Tenant that the individuals executing this Agreement on behalf of Landlord have a full power and authority to execute this Agreement on behalf of Landlord and to bind all parties comprising the Landlord.

IN WITNESS WHEREOF, this Agreement was executed as of the date set forth above.

	LANDLORD:
WITNESS:	MILTON J. ACKERMAN, ET AL
By: /s/ Michael A. Solberg ----------	By: /s/ Milton J. Ackerman ----------
Name: Michael A. Solberg	Name: Milton J. Ackerman Title: General Partner
WITNESS:	ATLANTIC PROPERTIES COMPANY
By: /s/ Michael A. Solberg ----------	By: /s/ Milton J. Ackerman ----------
Name: Michael A. Solberg	Name: Milton J. Ackerman Title: General Partner
ATTEST:	HALSEY DRUG CO., INC.
By: /s/ Carol Whitney Name: Carol Whitney Title: Vice President, Administration	By: /s/ Peter A. Clemens Name: Peter A. Clemens Title: Vice President and Chief Financial Officer

EXHIBIT A

(1) The Modification, Consolidation & Extension Agreement (the "Modification Agreement"), dated October 31, 1994, by and among Milton J. Ackerman, Sue Ackerman, Lee Hinderstein, Thelma Hinderstein and Marilyn Weiss, individuals doing business as Milton J. Ackerman, et al. and Atlantic Properties Company, collectively as landlord, and Tenant, as tenant, as amended by First Amendment to Modification, Consolidation and Extension Agreement, dated August 1, 1996, between Milton J. Ackerman, Sue Ackerman, Lee Hinderstein, Thelma Hinderstein and Marilyn Weiss, individuals doing business as Atlantic Properties Company, and Tenant, and Second Amendment to Modification, Consolidation and Extension Agreement, dated March 10, 1998, between Milton J. Ackerman, Sue Ackerman, Lee Hinderstein, Thelma Hinderstein and Marilyn Weiss, individuals doing business as Atlantic Properties Company, and Tenant, and to all of the leases and agreements incorporated therein and/or modified, consolidated and extended thereby (including, without limitation, the March 1985 Lease, the February 1988 Lease, the February 1989 Lease, the August 1989 Lease and the January 1990 Lease described below), and

(2) The Agreement of Lease (the "Additional Lease"), dated October 31, 1994, by and among Milton J. Ackerman, Sue Ackerman, Lee Hinderstein, Thelma Hinderstein and Marilyn Weiss, individuals doing business as Milton J. Ackerman, et al. and Atlantic Properties Company, collectively as landlord, and Tenant, as tenant.

Leases included in Modification Agreement

1. Lease (the "March 1985 Lease") dated March 26, 1985 between Milton J. Ackerman, Thelma Hinderstein and Marilyn Weiss, Landlord and Halsey Drug Co., Inc., Tenant as to the premises known as 1827-1829 Pacific Street, 1830 Atlantic Avenue, 1842 Atlantic Avenue, 1825 Pacific Street, 1828 Atlantic Avenue and 1824 Atlantic Avenue, Brooklyn, NY (collectively designated as Parcels A through F in said Lease) and between Milton J. Ackerman, Sue Ackerman, Lee Hinderstein, Thelma Hinderstein and Marilyn Weiss, Landlord and Halsey Drug Co., Inc., Tenant as to premises known as 1787 Dean Street and Block 1343 Lots 37, 38 and 29, Brooklyn, NY (collectively designated as Parcels G and H in said Lease).

2. Lease (the "February 1988 Lease") dated as of February 19, 1988 between Milton J. Ackerman, Sue Ackerman, Lee Hinderstein, Thelma Hinderstein and Marilyn Weiss, Landlord and Halsey Drug Co., Inc., Tenant for premises known as 1775 Dean Street, Brooklyn, NY.

3. Lease (the "February 1989 Lease") dated as of February 17, 1989 between Milton J. Ackerman, Thelma Hinderstein and Marilyn Weiss D/B/A Milton J. Ackerman, et al, Landlord and Halsey Drug Co., Inc., Tenant for approximately 7,500 square feet of space in a portion of the premises known as 1823 Pacific Street, Brooklyn, NY.

4. Lease (the "August 1989 Lease") dated as of August, 1989 between Milton

J. Ackerman, Sue Ackerman, Lee Hinderstein, Thelma Hinderstein and Marilyn Weiss D/B/A Milton J. Ackerman, et al, Landlord and Halsey Drug Co., Inc., Tenant for premises known as 1769-1773 Dean Street, Brooklyn, NY.

5. Lease (the "January 1990 Lease") dated as of January 1, 1990 between Milton J. Ackerman, Thelma Hinderstein and Marilyn Weiss D/B/A Atlantic Properties Company, Landlord and Halsey Drug Co., Inc., Tenant for premises known as 1838 Atlantic Avenue, Brooklyn, NY.

Exhibit 23.1

CONSENT OF INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS

We have issued our report dated March 30, 2000, accompanying the consolidated financial statements included in the Annual Report of Halsey Drug Co., Inc. on Form 10-K for the year ended December 31, 1999. We hereby consent to the incorporation by reference of said report in the Registration Statement of Halsey Drug Co., Inc. on Form S-8 (File NO. 33-98396, effective October 19, 1995).

/S/ GRANT THORNTON LLP
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GRANT THORNTON LLP

New York, New York
April 14, 2000

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THIS SCHEDULE CONTAINS SUMMARY FINANCIAL INFORMATION EXTRACTED FROM THE CONDENSED CONSOLIDATED STATEMENT OF FINANCIAL CONDITION AT DECEMBER 31, 199 AND THE CONDENSED CONSOLIDATED STATEMENT OF INCOME FOR THE YEAR ENDED DECEMBER 31, 199 AND IS QUALIFIED IN ITS ENTIRETY BY REFERENCE TO SUCH FINANCIAL STATEMENTS.

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