SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D. C. 20549

FORM 8-K

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

DATE OF REPORT (DATE OF EARLIEST EVENT REPORTED): DECEMBER 20, 2002

HALSEY DRUG CO., INC.

695 NORTH PERRYVILLE ROAD, ROCKFORD, ILLINOIS 61107

(815-399-2060)

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

ITEM 5. OTHER EVENTS

DEBENTURE OFFERING

On December 20, 2002, Halsey Drug Co., Inc. (the "Company") consummated a private offering of securities for an approximate aggregate purchase price of $26,385,000 (the "Offering"). The securities issued in the Offering consisted of 5% convertible senior secured debentures (the "Debentures"). The Debentures were issued by the Company pursuant to a certain Debenture Purchase Agreement dated December 20, 2002 (the "Purchase Agreement") by and among the Company, Care Capital LLC ("Care Capital"), Essex Woodlands Health Ventures V ("Essex"), Galen Partners III, L.P. and each of the Purchasers listed on the signature page thereto (collectively, the "2002 Debenture Investor Group").

Of the $26,385,000 million in Debentures issued in the Offering, approximately $15,885,000 of Debentures were issued in exchange for the surrender of like amount of principal and accrued interest outstanding under the Company's 10% convertible promissory notes issued pursuant to various working capital 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 lenders, during the period from August 15, 2001 through and including December 20, 2002.

The Debentures, issued at par, will become due and payable as to principal on March 31, 2006. Interest on the principal amount of the Debentures, at the rate of 5% per annum, is payable on a quarterly basis. With the exception of the Debentures issued to Care Capital, interest will be paid by the Company's issuance of a debenture instrument substantially identical to the Debentures issued in the Offering, in the principal amount equal to the accrued interest for each quarterly period (the "Interest Debentures"). Debentures issued to Care Capital provide that fifty percent (50%) of the interest payments under such Debentures will be satisfied in cash with the balance satisfied by the Company's issuance of Interest Debentures.

The Debentures issued to each of Care Capital and Essex are convertible at any time after issuance into shares of the Company's Common Stock, $.01 per value per share (the "Common Stock"). The Debentures issued to Galen and the other investors in the Offering (excluding Care Capital and Essex) are convertible at any time after the approval of the Company's shareholders and debentureholders of an amendment to the Company's Certificate of Incorporation to increase its authorized shares of Common Stock from 80,000,000 shares to such number of shares as shall provide sufficient authorized shares to permit the conversion of such Debentures and Company's outstanding convertible securities, as provided in the Purchase Agreement (see "Voting Agreement" below). Subject to the foregoing, the Debentures are convertible into shares of Common Stock at a price per share (the "Conversion Price") of $ .34. Until such time as the Company competes a Subsequent Material Offering (as defined below) the Conversion Price is subject to adjustment, from time to time, to equal the consideration per share received by the Company for its Common Stock, or the conversion/exercise price per share of the Company's Common Stock issuable under rights or options for the purchase of, or stock or other securities convertible into, Common Stock

("Convertible Securities"), if lower than the then applicable Conversion Price. Following the Company's completion of a Subsequent Material Offering, the Conversion Price is subject to adjustment from time to time on a weighted-average dilution basis. A "Subsequent Material Offering" is the grant or issuance of Common Stock or Convertible Securities by the Company during any six month period for an aggregate gross consideration of at least $10,000,000. The Conversion Price is also subject to adjustment to give effect to additional Debentures, if any, that may be issued under the Purchase Agreement and in the event of a subsequent recapitalization of the Company's outstanding common stock purchase warrants issued to Galen in consideration for various bridge loans to the Company.

The Interest Debentures are convertible at any time after issuance into shares of Common Stock at a price per share equal to the average of the closing bid and asked prices of the Common Stock for the twenty (20) trading days immediately preceding the applicable interest payment date under the Debentures, as reported by the Over-the-Counter ("OTC") Bulletin Board.

Assuming the conversion of the Debentures at the initial Conversion Price of $ .34 per share, the Debentures are convertible into an aggregate of approximately 77,602,000 shares of the Company's Common Stock.

The Purchase Agreement provides that the holders of the Debentures shall have 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. Each Debenture holder shall have such number of votes as shall equal the number of votes he would have had if such holder converted the entire outstanding principal amount of his Debenture into shares of Common Stock immediately prior to the record date relating to such vote; provided, however, that any Debentures held by Care Capital shall, for so long as they are held by Care Capital, have no voting rights. The Purchase Agreement also provided for the execution of a Debentureholder Agreement providing the holders of the Debentures with veto rights relating to certain material Company transactions as further described under the caption "Debentureholders Agreement" below.

The Purchase Agreement provides that each of Care Capital and Essex has the right to designate for nomination a person to be a member of the Company's Board of Directors as of the closing date of the Offering (collectively, the Designees"). The Purchase Agreement further provides that the Designees shall be, if so requested by such Designee in its sole discretion, appointed to the Company's Executive Committee, Compensation Committee and any other Committee of the Board of Directors. Accordingly, effective as of the closing of the Purchase Agreement, the Board of Directors appointed each of Jerry Karabelas and Immanuel Thangaraj to the Company's Board of Directors. The Company has agreed to nominate and appoint to the Board of Directors, subject to shareholder approval, one designee of each of Care Capital and Essex for so long as each holds the Debentures.

The Company is a party to a certain Loan Agreement with Watson Pharmaceuticals, Inc. ("Watson") pursuant to which Watson has made a term loan to the Company in the principal amount of $17,500,000 (the "Watson Loan Agreement"). It was a condition to the completion of the Offering that the Watson Loan Agreement and related agreements with Watson be amended. See "Watson Loan Agreement Amendments" below for a description of the amendments to the Watson Loan Agreement.

As part of the closing of the Purchase Agreement, the Company and certain holders of common stock purchase warrants issued in prior Company debenture offerings in 1998 and 1999 and pursuant to bridge loan transactions during the period 1998 through 2002, executed a certain Warrant Recapitalization Agreement providing for the recapitalization of approximately 8,145,736 warrants in exchange for the issuance of an aggregate of 5,970,083 shares of the Company's Common Stock (see "Warrant Recapitalization" below).

Additional Terms of the Purchase Agreement, Debentures and Warrants

Debentureholders Agreement

As part of the closing of the Purchase Agreement, the Company and the purchasers of the Debentures executed a certain Debentureholders Agreement providing, among other things, that the approval of the holders of at least sixty six and two-thirds percent (66 2/3%) of the aggregate principal amount of the Debentures is required to authorize (a) any modification of the rights of the holders of the Debentures, (b) any issuance of securities of the Company which rank senior or pari passu to the Debentures, (c) any dividends or distributions on, or redemption of, any securities ranking junior in priority to the Debentures, other than dividends or distributions payable in the Company's Common Stock or cash interest paid to individual investors in the Company's 5% convertible senior secured debentures issued pursuant to that certain Debenture and Warrant Purchase Agreement (the "1998 Purchase Agreement") between the Company, Galen Partners III, L.P. and the other signatories thereto, dated March 10, 1998 (the "Galen Group Debentures") and issued pursuant to the Debenture and Warrant Purchase Agreement (the "1999 Purchase Agreement") between the Company, Oracle Strategic Partners, L.P. and the other signatories thereto, dated May 26, 1999 (the "Oracle Group Debentures" and together with the Galen Group Debentures, the "Existing Debentures"), (d) the merger or consolidation of the Company, the sale, transfer, lease or other disposition of all or substantially all of the Company's consolidated assets, or the liquidation, recapitalization or reorganization of the Company, other than any such transaction where the cash, securities and/or other liquid consideration received for the voting stock of the Company in such transaction is at least four (4) times the then applicable conversion price of the Debentures, (e) any increase in the number of members comprising the Company's Board of Directors above eleven (11) members, and (f) the consummation of a strategic alliance, business combination, licensing arrangement or other corporate partnering involving the issuance by the Company of in excess of $10,000,000 in equity securities of the Company.

The Debentureholders Agreement further provides that the holders of at least sixty six and two-thirds percent (66 2/3%) of the aggregate principal amount of the Debentures and Existing Debentures is required in order to authorize (a) any amendment to the Company's Certificate of Incorporation, (b) dividends or distributions on, or redemptions of, any securities ranking junior to the Existing Debentures, other than distributions or dividends payable in the Company's capital stock or cash interest paid to individual investors in the Existing Debentures, (c) any issuance of the Company's securities ranking senior or pari passu to the Existing Debentures, and (d) the completion of any transaction described in subsections (d), (e) and (f) in the preceding paragraph.

Voting Agreement

The Company is obligated under the Purchase Agreement to solicit shareholder approval to amend its Certificate of Incorporation to (i) provide the holders of the Debentures with "as converted" voting rights; and (ii) to increase its authorized shares of Common Stock from 80,000,000 to such number of shares as shall provide sufficient authorized shares to permit the conversion of the Debentures and the exercise and conversion of the Company's outstanding convertible securities, including the Watson Warrant (as defined under the caption "Watson Loan Agreement Amendments" below)(the "Charter Amendments"). The Company anticipates soliciting shareholder approval for the Charter Amendments at its upcoming 2003 Annual Meeting of Shareholders. In this regard, as part of the closing of the Purchase Agreement, each of Galen Partners III, L.P., Galen Partners International III, L.P., Galen Employee Fund III, L.P., Oracle Strategic Partners, L.P., Michael Reicher, the Company's Chief Executive Officer and Peter Clemens, the Company's Chief Financial Officer (collectively, the "Voting Agreement Parties") executed a Voting Agreement dated December 20, 2002 pursuant to which each agreed to vote all of their respective voting securities of the Company in favor of the Charter Amendments. The voting securities held by the Voting Agreement Parties represents an aggregate of approximately 64% of the voting rights under the Company's outstanding voting securities.

Right of First Refusal

The Purchase Agreement provides the holders of the Debentures and the holders of shares of Common Stock issued upon conversion of the Debentures (provided the Debentures remain outstanding and the shares received upon conversion have not been sold, transferred or otherwise disposed of) as well as the holders of the Galen Group Debentures with a right of first refusal relating to any subsequent issuance, sale or exchange of any shares of the Company's Common Stock or convertible securities, exclusive of certain excluded securities and offerings in an amount less than $200,000.

Secured Debt

The Debentures are secured by a lien on all assets of the Company, tangible and intangible. In addition, each of Houba, Inc. and Halsey Pharmaceuticals, Inc., each a wholly-owned subsidiary of the Company, has executed in favor of the 2002 Debenture Investor Group an Unconditional Agreement of Guaranty of the Company's obligations under the Purchase Agreement. Each Guaranty is secured by all assets of such subsidiary, and, in the case of Houba, Inc., by a mortgage lien on its real estate. In addition, the Company has pledged the stock of each such subsidiary to the 2002 Debenture Investor Group to further secure its obligations under the Purchase Agreement.

In accordance with the terms of a Subordination Agreement dated December 20, 2002 between the Company, the holders of the Debentures, the holders of the Existing Debentures and Watson, the liens on the Company's and its Subsidiaries' assets as well as the payment priority of the Debentures are (i) subordinate to the Company's lien and payment obligations in favor of Watson under the Watson Loan Agreement, and (ii) senior to the Company's lien and payment obligations in favor of the holders of the Existing Debentures in the aggregate principal amount of approximately $50,723,938. In addition to the subordination of the liens and the payment priority of the Existing Debentures in favor of the Debentures issued in the Offering, as part of the completion of the Offering, each of the holders of the Galen Group Debentures and the Oracle Group Debentures agreed to extend the maturity date of the Existing Debentures from March 15, 2003 to March 31, 2006.

Conversion of Debentures at Company's Option

Provided that no event of default relating to a failure to pay principal and interest under the Debentures shall exist and then be continuing, in the event that following December 20, 2005, (i) the average of the closing bid and asked prices per share of the Company's Common Stock, as reported by the OTC Bulletin Board (or the closing price per share as reported by the NASDAQ National Market or any Exchange on which the shares may then be traded) exceeds the product of (x) the then applicable Conversion Price of the Debentures, multiplied by (y) four (4), for each of the twenty (20) consecutive trading days during which the average daily trading volume for such twenty (20) trading day period is at least one million dollars ($1,000,000), or (ii) the Company shall have obtained the written consent of the holders of 75% of the principal amount of the Debentures then outstanding to convert the Debentures into Common Stock, then the Company may upon written notice to the holders of the Debentures require that all, but not less than all, of the outstanding principal amount of the Debentures be converted into shares of the Company's Common Stock at a price per share equal to the Conversion Price of the Debentures (as such Conversion Price may be adjusted pursuant to the terms of the Purchase Agreement).

Registration Rights

As part of the closing of the Purchase Agreement, the Company executed in favor of the holders of the Debentures, the holders of the Existing Debentures, the holders of shares received in the Warrant Recapitalization Agreement (as described below under the caption "Warrant Recapitalization") and Watson, a Registration Rights Agreement providing for (i) the termination of the registration rights granted to the holders of the Existing Debentures under the 1998 Purchase Agreement and the 1999 Purchase Agreement, (ii) the termination of the registration rights granted to Galen relating to the common stock purchase warrants issued to Galen in consideration for various bridge loans to the Company (the "Galen Warrants"), and (iii) the grant of registration rights to Watson, the holders of the Debentures, the holders of the Existing Debentures, the holders of shares of common stock received pursuant to the Warrant Recapitalization Agreement (the "Warrant Recap Shares"), and Galen as holder of the Galen Warrants, to register under the Securities Act of 1933, as amended, the Warrant Recap Shares, the shares issuable on exercise of the Watson Warrant and the Galen Warrants, and the shares issuable on conversion of the Debentures and the Existing Debentures (collectively, the "Registrable Securities"). The Registration Rights Agreement provides each of Galen and Watson with two (2) demand registrations on Form S-1 (or any successor form) and the holders of 20% of the Registrable Securities with one (1) demand registration on Form S-1 (or any successor form). The Registration Rights Agreement also provides such parties with unlimited piggyback registration rights.

Other Terms

The Purchase Agreement contains other customary terms and provisions, including, without limitation, customary representations and warranties, affirmative covenants, negative covenants and requirements for the provision of certain financial information during the term that the Debentures remain outstanding, all of which are customary for the type of securities issued in the Offering.

Reference is made to the Company's Press Release dated December 20, 2002 which describes, among other things, the completion of the Offering. The Press Release is hereby incorporated by this reference and is included as Exhibit 99.1 hereto.

WATSON LOAN AGREEMENT AMENDMENTS

As part of the closing of the Offering, the Watson Loan Agreement was amended to (i) extend the maturity date of the Watson Loan Agreement from March 31, 2003 to March 31, 2006, and (ii) increase the principal amount of the Watson Term Loan from $17,500,000 to $21,401,331 to reflect the inclusion of approximately $3,901,331 owed by the Company to Watson under a product supply agreement between the parties.

In consideration for the amendment to the Watson Loan Agreement, the Company issued to Watson a Common Stock Purchase Warrant exercisable for 10,700,665 shares of the Company's

Common Stock (the "Watson Warrant"). The Watson Warrant has a term expiring December 31, 2009 and has an exercise price of $ .34 per share. Watson is also a party to the Registration Rights Agreement described above under the caption "Registration Rights".

WARRANT RECAPITALIZATION

As part of the completion of the transactions contemplated in the Purchase Agreement, the Company consummated the terms of a Warrant Recapitalization Agreement dated December 20, 2002 (the "Recapitalization Agreement") between the Company and certain holders of an aggregate of 8,145,736 Common Stock Purchase Warrants issued by the Company (i) pursuant to that certain Debenture and Warrant Purchase Agreement dated March 10, 1998 between the Company and the purchasers listed on the signature page thereto (the "1998 Warrant"), (ii) pursuant to that certain Debenture and Warrant Purchase Agreement dated May 26, 1999 between the Company and the purchasers listed on the signature page thereto (the "1999 Warrant"), and (iii) pursuant to various bridge loan transactions during the period from 1998 through 2002 (the "Bridge Loan Warrants" and collectively with the 1998 Warrants and 1999 Warrants, the "Recapitalization Warrants"). As part of the closing of the Recapitalization Agreement, the warrantholders as a party thereto surrendered to the Company for cancellation the Recapitalization Warrants in exchange for the issuance of an aggregate of 5,970,083 shares of Common Stock.

ITEM 7. FINANCIAL STATEMENTS AND EXHIBITS.

(b) EXHIBITS

EXHIBIT NUMBER	DESCRIPTION
4.1	Form of 5% Convertible Senior Secured Debenture.
10.1	Debenture and Warrant Purchase Agreement by and among Halsey Drug Co., Inc., Care Capital LLC, Essex Woodlands Health Ventures V and the other Purchasers listed on the signature page thereto.
10.2	Form of General Security Agreement of Halsey Drug Co., Inc.
10.3	Form of Agreement of Guaranty of Subsidiaries of Halsey Drug Co., Inc.
10.4	Form of Guarantor General Security Agreement.
10.5	Stock Pledge Agreement by and between Halsey Drug Co., Inc. and Care Capital LLC, as agent.

10.6	Voting Agreement.
10.7	Debentureholders Agreement.
10.8	Amendment to Debenture and Warrant Purchase Agreement between Halsey Drug Co., Inc., Galen Partners III, L.P. and other signatories thereto, amending the Debenture and Warrant Purchase Agreement dated March 10, 1998 between the Company, Galen Partners III, L.P. and the other signatories thereto.
10.9	Amendment to Debenture and Warrant Purchase Agreement between Halsey Drug Co., Inc., Oracle Strategic Partners, L.P. and the other signatories thereto, amending the Debenture and Warrant Purchase Agreement dated May 26, 1999 between the Company, Oracle Strategic Partners, L.P. and the other signatories thereto.
10.10	Amended and Restated 5% Convertible Senior Secured Debenture due March 31, 2006.
10.11	Second Amendment to Loan Agreement between Halsey Drug Co., Inc. and Watson Pharmaceuticals, Inc., amending the Loan Agreement dated March 29, 2000 between Halsey Drug Co., Inc. and Watson Pharmaceuticals, Inc.
10.12	Secured Promissory Note issued by Halsey Drug Co., Inc. in favor of Watson Pharmaceuticals, Inc. in the principal amount $17,500,000.
10.13	Secured Promissory Note issued by Halsey Drug Co., Inc. in favor of Watson Pharmaceuticals, Inc. in the principal amount of $3,901,331.
10.14	Second Amendment to Finished Goods Supply Agreement (Core Products) between Halsey Drug Co., Inc. and Watson Pharmaceuticals, Inc. amending the Finished Goods Supply Agreement (Core Products) dated March 29, 2000.
10.15	Watson Common Stock Purchase Warrant.
10.16	Registration Rights Agreement.
10.17	Warrant Recapitalization Agreement.
99.1	Press Release of Halsey Drug Co., Inc. dated December 23, 2002.

SIGNATURES

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

HALSEY DRUG CO., INC.

By: /s/ Peter A. Clemens

Peter A. Clemens
Vice President & Chief Financial Officer

Date: December 27, 2002

EXHIBIT INDEX

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10.3	Form of Agreement of Guaranty of Subsidiaries of Halsey Drug Co., Inc.
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EXHIBIT 4.1

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 31, 2006

$_____ No. N-__
December 20, 2002

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 _____, or registered assigns (the "Payee" or "Holder"), upon due presentation and surrender of this Debenture, on March 31, 2006 (the "Maturity Date"), the principal amount of _____ ($_____) and accrued interest thereon as hereinafter provided.

This Debenture was issued by the Company pursuant to a certain Debenture Purchase Agreement dated as of December __, 2002 among the Company and certain purchasers identified therein, 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 due March 31, 2006 (together with the Interest Payment Debentures referred to below) (the "Debentures") in the aggregate principal amount of $_____. The holders from time to time of the Debentures (including the Holder) are referred to hereinafter as the "Holders". The Holder is entitled to the benefits of the Purchase Agreement, including, without limitation, the rights upon the occurrence and during the continuance of an Event of Default and the benefits of security interests and guaranties referred to below. Reference is made to the Purchase Agreement and the documents entered into pursuant thereto with respect to certain additional rights of the Holder and obligations of the Company and its Subsidiaries not expressly set forth herein. Capitalized terms used herein but not otherwise defined herein shall have the meaning ascribed thereto in the Purchase Agreement. All such rights and obligations set forth in the Purchase Agreement are incorporated herein by reference.

ARTICLE I

PAYMENT OF PRINCIPAL AND INTEREST; METHOD OF PAYMENT

1.1. Payment of the principal on this Debenture shall be made in cash, in immediately available funds, 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) shall accrue on the unpaid portion of said principal amount from time to time outstanding at the rate of five percent (5%) per annum (the "Stated Interest Rate"), and shall be paid by the Company to the Payee at three (3) month intervals, on each January 1, April 1, July 1 and October 1 during the term of this Debenture, commencing January 1, 2003, and on the Maturity Date (each such date being an "Interest Payment Date") and on the dates specified therefor in Article III hereof. The payment of accrued interest on this Debenture shall be made in the form of 5% convertible senior secured debentures (each, an "Interest Payment Debenture") identical in all respects to this Debenture; provided, however, that (i) the principal amount of such Interest Payment Debenture upon issuance shall be the accrued and unpaid interest for the immediately preceding calendar quarter, (ii) the date of such Interest Payment Debenture shall be its issue date, and (iii) the Conversion Price (as defined in Section 3.1(a) hereof) of such debenture shall equal the average of the closing bid and asked prices for the Company's Common Stock as reported in the Over-the-Counter Bulletin Board ("OTC Bulletin Board")(or such other over-the-counter market or exchange on which the Company's Common Stock may then be traded or admitted for trading) for the twenty (20) trading days immediately preceding the date of such interest payment. No cash interest payments will be made on this Debenture, except on the Maturity Date pursuant to the terms of the Interest Rate Debentures. Both principal hereof and interest hereon 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 by check or wire transfer, at the Holder's election, and interest in the form of an Interest Payment Debenture, 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, (except to the extent otherwise specified herein) interest or both shall remain unpaid for a period of two (2) business days or more, a late charge equivalent to five (5%) percent of each installment shall be charged and may be satisfied by the Company's issuance of an Interest Payment Debenture having a principal amount which includes such late charge. 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/SUBORDINATION

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 Holder and the other Holders pursuant to a General Security Agreement dated as of December __, 2002, and the 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 and delivered in favor of the Holder and the other Holders a Continuing Unconditional Guaranty, dated an even date herewith (each a "Guarantee"), guaranteeing the full and unconditional payment when due of the amounts payable by the Company to the Holder and the other Holders pursuant to the terms of their respective Debentures. The obligations of each Guarantor under its Guaranty are secured (subject to the Subordination Agreement) pursuant to security interests on and collateral assignments of, assets, tangible and intangible, of such Guarantor granted by the Guarantor to the Holder and the other Holders pursuant to a security agreement dated as of December __, 2002, and the collateral assignments referred to in the Purchase Agreement. The obligations of Houba under its Guaranty are also secured (subject to the Subordination Agreement) pursuant to a mortgage on real property located at 16235 State Road 17, Culver, Indiana. The rights of the Holders with respect to the collateral described in the security agreements and collateral assignments with the Company and the Guarantors as provided in the Purchase Agreement are subject to the terms of the Subordination Agreement dated of even date herewith by and among the Company, Watson Pharmaceuticals, Inc., the Holders and the other signatories thereto.

ARTICLE III

CONVERSION

3.1. Conversion at Option of Holder. At any time after the Shareholders Meeting Date,(the "Initial Conversion Date") until the earlier of (a) the Maturity Date or (b) 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 $____ per share, as such conversion price may be adjusted as provided in Sections 3.5, 3.6 and 3.7 hereof (as so adjusted) (the "Conversion Price"). 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 Sections 3.5, 3.6 and 3.7 hereof. Not later than three (3) days 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.

For purposes hereof the term "Shareholders Meeting Date" shall mean that date on which the shareholders and the debentureholders amend the Company's Certificate of Incorporation to increase the number of authorized shares of the Company's Common Stock available for issuance from 80,000,000 to such number of shares as shall equal the sum of (i) the Company's issued and outstanding Common Stock, plus (ii) the number of shares of Common Stock issuable upon the conversion and exercise of the Company's outstanding convertible securities, plus (iii) the number of shares of Common Stock issuable upon conversion of the Debentures and exercise of the Watson Warrant , plus (iv) 50 million shares, as shall sum shall be rounded up to the nearest whole five million shares.

3.2. Conversion at Option of the Company. So long as an Event of Default as provided in Section 12.1(a) of the Purchase Agreement (concerning the Company's failure to pay principal and interest under the Debentures) shall not have occurred and be continuing, in the event that following December __, 2005, (i) the average of the closing bid and asked prices per share of the Company's Common Stock as reported by the OTC Bulletin Board (or such other exchange or over-the-counter market on which the Shares may then be listed or admitted for trading) exceeds the product of (x) the then Applicable Conversion Price (as defined in Section 3.7 hereof), multiplied by (y) four (4), such average of bid and ask prices to be determined for each of twenty (20) consecutive trading days in which the average daily trading volume for such twenty (20) trading day period exceeds one million dollars ($1,000,000) (based on the number of Shares traded multiplied by the average of the closing bid and asked prices), or (ii) the Company shall have obtained the written consent of the Holders of at least 75% of the principal amount of the Debentures then outstanding to convert the Debentures into Common Stock, 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 then in effect. The Mandatory Conversion Notice shall state (a) the date fixed for conversion (the "Conversion Date") (which date shall not be prior to the date the Mandatory Conversion Notice is given), (b) any disclosures required by law, (c) the trading dates and closing prices of the Common Stock giving rise to the Company's option to

require conversion of the Debenture, (d) that the Debentures shall cease to accrue interest after the day immediately preceding the Conversion Date, (e) the place where the Debentures shall be delivered and (f) 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 (i) to whom notice was not mailed or (ii) 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, not later than three (3) days following the surrender of this Debenture the Company shall issue and deliver 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 Company has reserved the remaining balance of its authorized but unissued and unreserved shares of Common Stock to permit the conversion of the Debentures to the extent of its current unissued and unreserved authorized Common Stock. In accordance with the provisions of Section 9.12 of the Purchase Agreement, the Company covenants to seek the approval of its shareholders and directors to amend its Certificate of Incorporation (i) to increase its authorized shares from 80,000,000 to such number of shares as shall equal the sum of (A) the Company's issued and outstanding Common Stock, plus (B) the number of shares of Common Stock issuable upon the conversion and exercise of the Company's outstanding convertible securities, plus (C) the number of shares

of Common Stock issuable upon conversion of the Debentures and exercise of the Watson Warrant, plus (D) 50 million shares, as such sum shall be rounded up to the nearest whole five million shares, and (ii) to provide voting rights to the Holders on an as converted basis as a single class with the holders of the Common Stock. 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 shares of 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, if any, upon which the Common Stock may then be listed.

3.5. Dividends; Reclassifications, etc. In the event that the Company shall, at any time prior to the earlier to occur of (a) exercise of conversion rights hereunder and (b) 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 shall receive, in addition to 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.

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

(a) Until such time as the Company completes a Subsequent Material Offering (as defined in Section 3.7(d) hereof), if 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"), including in connection with a Subsequent Material Offering, other than:

(i) shares issued in a transaction described in subsection (c) 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 Conversion Price in effect immediately prior to such issuance or sale (the "Applicable Conversion Price"), then the Applicable Conversion Price in effect immediately prior to such issuance or sale shall, and thereafter, except as otherwise provided in Subsection 3.7 (b) hereof, upon each issuance or sale for a consideration per share which is less than the Applicable Conversion Price, the Applicable Conversion Price shall, simultaneously with such issuance or sale, be adjusted, so that such Applicable Conversion Price shall equal (A) the price per share received by the Company, in the case of the issuance of Common Stock by the Company, or (B) the exercise or conversion price of the Convertible Securities issued by the Company, as applicable.

(b) If at any time following the Company's completion of a Subsequent Material Offering the Company shall grant or issue any shares of Common Stock, or grant or issue any Convertible Securities, other than:

(i) shares issued in a transaction described in subsection (c) 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 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 the Applicable Conversion Price shall equal a price determined by multiplying the Applicable Conversion Price by a fraction, of which:

(A) the numerator shall be the sum of (i) the total number of shares of Common Stock outstanding when the Applicable Conversion Price became effective, plus (ii) the number of shares of Common Stock which the aggregate consideration received, as determined in accordance with Subsection 3.7(e), 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(f), 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(b)) at the Fair Market Value of the Common Stock; and

(B) the denominator shall be the total number of Shares of Common Stock outstanding (or deemed to be outstanding as provided in Subsection 3.7(f) hereof) immediately after the issuance or sale of such additional shares.

For purposes of this Section 3.7, "Fair Market Value", in respect of any such issuance or sale, 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, during such period, shares of Common Stock are not listed on a national securities exchange but are quoted on the National Association of Securities Dealers Automatic Quotation System ("NASDAQ") National Market System, the closing price per share as reported by 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 solely pursuant to this Section 3.7(b), the Holder shall thereafter be entitled to acquire upon conversion under Section 3.1 or Section 3.2, at the Applicable Conversion Price, 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.

(c) 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 each 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 or Convertible Securities issued in satisfaction of interest payments on the Debentures and the Existing Debenture (as defined in the Purchase Agreement), including the issuance of Common Stock or Convertible Securities issued in satisfaction of interest payments on debenture instruments issued by the Company in satisfaction of the interest payments on the Debentures and Existing Debentures; or

(iv) the issuance of any shares of Common Stock pursuant to the grant or exercise of Convertible Securities outstanding as of the date hereof, including, without limitation, the Debentures (as defined in the Purchase Agreement) (exclusive of any subsequent amendments thereto); or

(v) the issuance of shares of Common Stock pursuant to the Recapitalization Agreement.

(d) For purposes hereof, "Subsequent Material Offering" shall mean the grant or issuance of shares of Common Stock, or the grant or issuance of Convertible Securities, during any six (6) month period for an aggregate gross consideration (determined in accordance

with Subsection 3.7 (e) hereof) of at least ten million dollars ($10,000,000) for a consideration per share that is in excess of the then Applicable Conversion Price.

(e) For the purpose of Subsections 3.7(a), 3.7(b) and 3.7(d), 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 exchanged 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.

(f) For purposes of the adjustment provided for in Subsections 3.7(a) and 3.7(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.

(g) 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(g) for all transactions (which would have affected such adjusted Conversion Price) made after the issuance or sale of such Convertible Securities.

(h) 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 one cent per share in such Conversion Price; provided, however, that any adjustments which by reason of this subsection 3.7(h) 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.

(i) 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 in the Purchase Agreement all amounts then remaining unpaid on this Debenture may be declared to be, or automatically become, 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; Specific Performances. 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. Without limiting the generality of the foregoing, the Company and Holder acknowledge and agree that the transactions contemplated by this Debenture are unique. Accordingly, the Company acknowledges and agrees that in addition to the other remedies to which the Holder may be entitled, the Holder shall be entitled to a decree of a specific performance and injunctive and other equitable relief to require the Company's compliance with its obligations hereunder.

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. Subject to the terms of the Purchase Agreement, no modification or waiver of any provision of this Debenture shall be effective unless it shall be in writing and signed by the Holder, and any such modification or waiver shall apply only in the specific instance for which given.

4.6. Governing Law; Jurisdiction. (a) This Debenture and the rights of the holders hereof shall be governed by, and construed in accordance with, the laws of the State of New York wherein the terms of this Debenture were negotiated, excluding to the greatest extent permitted by law any rule of law that would cause the application of the laws of any jurisdiction other than the State of New York.

(b) The undersigned hereby irrevocably and unconditionally submits, for itself and its property, to the nonexclusive jurisdiction of any New York State court or United States Federal court sitting in New York City, and any appellate court from any thereof, in any action or proceeding arising out of or relating to this Debenture or for recognition or enforcement of any judgment, and each of the parties hereto irrevocably and unconditionally agrees that all claims in respect of any such action or proceeding may be heard and determined in any such New York State court or, to the fullest extent permitted by law, in such United States Federal court. The undersigned agrees that a final judgment in any such action or proceeding shall be conclusive and may be enforced in other jurisdictions by suit on the judgment or any other manner provided by law. Nothing in this Debenture or any other Transaction Document shall affect any right that any party may otherwise have to bring any action or proceeding relating to this Debenture or any of the other Transaction Documents in the courts of any jurisdiction.

(c) The Company irrevocably and unconditionally waives, to the fullest extent it may legally and effectively do so, any objection that it may now or hereafter have to the laying of venue of any suit, action or proceeding arising out of or in relation to this Debenture or any other transaction document to which it is a party in any such New York State or United States Federal Court. The Company hereby irrevocably waives, to the fullest extent permitted by law, the defense of an inconvenient forum to the maintenance of such action or proceeding in any such court.

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

4.8. Successors. The term "Payee" and "Holder" as used herein shall be deemed to include the Holder 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.

4.13. WAIVER OF JURY TRIAL. THE COMPANY IRREVOCABLY WAIVES ALL RIGHT TO TRIAL BY JURY IN ANY ACTION, PROCEEDING OR COUNTERCLAIM (WHETHER BASED ON CONTRACT, TORT OR OTHERWISE) ARISING OUT OF OR RELATING TO THIS DEBENTURE OR ANY OTHER TRANSACTION DOCUMENT TO WHICH IT IS A PARTY IN THE NEGOTIATION, ADMINISTRATION, PERFORMANCE OR ENFORCEMENT THEREOF.

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:_____
Name: Michael Reicher
Title: Chief Executive Officer

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 31, 2006 evidenced hereby and hereby irrevocably appoints _____ 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

EXHIBIT 10.1

DECEMBER 20, 2002

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 (capitalized terms used in this Agreement without definition have the meanings assigned to them in Article XX):

ARTICLE I

AUTHORIZATION OF THE SECURITIES;
ADJUSTMENT OF CONVERSION PRICE

1.1. Authorization of Securities. (a) The Company represents that it has taken all corporate action necessary to authorize the issuance and sale of its 5% Convertible Senior Secured Debentures due March 31, 2006 in the aggregate principal amount of up to $35 million substantially in the form of Exhibit B hereto (such Debentures, together with the Debenture instruments evidencing interest payments on the Debentures in accordance with Section 1.1, as they may be amended, supplemented or otherwise modified from time to time in accordance with their terms, the "Debentures" or the "Securities").

(b) The Debentures are to be sold severally, and not jointly, pursuant to this Agreement to you (each of you is sometimes referred to herein as a "Purchaser").

(c) Interest on the Debentures (including on Debenture instruments issued pursuant to this sentence) is payable at the rate of 5% per annum in the form of Debenture instruments substantially identical to the Debentures; provided, however, that fifty percent (50%) of the interest payments payable under the Debentures issued to Care Capital Investments II, LP shall be paid in cash with the balance of such interest payments payable in like Debentures, all as more particularly specified in the Debenture. Each Debenture held by Galen, Galen Partners International III, L.P., Galen Employee Fund III, L.P. and any Additional Investor, or any affiliate thereof is convertible, at any time after the Shareholders Meeting Date, (i) in whole or in part at any time or from time to time at the option of the holder of such Debenture into a number of shares of the Company's Common Stock (the "Common Stock") initially at the rate of one share of Common Stock for each $.34 in principal amount of the respective Debenture to be converted and (ii) following the third anniversary of the issuance of the respective Debenture, in whole at the option of the Company in the circumstances set forth in Section 3.2 of the respective Debenture. Each Debenture held by Care Capital Investments II, LP or Essex Woodlands Health Ventures Fund V is convertible (i) in whole or in part at any time or from time to time at the option of the holder of such Debenture into a number of shares of Common Stock initially at the rate of one share of Common Stock for each [$___] in principal amount of the respective Debenture to be converted and (ii) following the third anniversary of the issuance of the respective Debenture, in whole at the option of the Company in the circumstances set forth in Section 3.2 of the respective Debenture. 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. The term Shares does not include any other shares of Common Stock or other capital stock of the Company.

(d) The Company and the Purchasers acknowledge and agree that the conversion price of the Debentures shall be calculated on the Closing Date and on any subsequent issuance of Debentures pursuant to Article III hereof (i) based on a fully-diluted valuation of the Company of $47.4 million prior to the Closing of the transactions provided in this Debenture Purchase Agreement, assuming a per share value of Common Stock equal to the conversion price of the Debentures, and (ii) to provide that the Debentures issued to the Purchasers shall be convertible into such number of Shares as shall represent forty two and four tenths percent (42.4%) (the "Aggregate Ownership Percentage") of the Company's Common Stock on the Closing Date, assuming the Company's issuance of Debentures in an aggregate principal amount of $35 million. The Aggregate Ownership Percentage shall be proportionately adjusted to the extent the Company issues Debentures in an aggregate principal amount less than $35 million. For purposes of the foregoing calculations, excluding common stock purchase options exercisable for up to 5,031,950 shares of Common Stock issued and outstanding on the Closing Date and listed on Section 1.1 of the Schedule of Exceptions, all shares of Common Stock underlying any convertible debentures, warrants, options and other convertible securities of the Company outstanding at the Closing Date shall be included, including, without limitation, the Watson Warrant, after giving effect to any change in the number of shares of Common Stock issuable under such convertible securities as a result of the completion of the transactions set forth in this Debenture Purchase Agreement and the application of the anti-dilution provisions contained in any such convertible securities.

1.2. Adjustment of Conversion Price. (a) The prices at which Shares may be acquired upon conversion of the Debentures are subject to adjustment as set forth in the Debentures. Without limiting the anti-dilution provisions contained in the Debentures, including, without limitation, Section 3.7 thereof, the Purchasers and the Company acknowledge and agree that in the event the common stock purchase warrants described in Exhibit O hereto exercisable for an aggregate of 11,475,116 shares of Common Stock (collectively, the "Remaining Galen Warrants") are exercised, converted, recapitalized or otherwise exchanged or substituted (the "Warrant Exchange Transaction") on or before December 15, 2003 for an aggregate number of shares which is less than or greater than 11,475,116 shares of Common Stock, the conversion price of the Debentures shall be adjusted in order to provide that the number of Shares issuable upon conversion of the Debentures shall equal the Aggregate Ownership Percentage as if the Warrant Exchange Transaction had been completed immediately prior to the Closing Date and the Company had issued the resulting shares of Common Stock in such transaction as of the Closing Date.

(b) In accordance with Article III hereof, the Company, from time to time, may issue additional Debentures pursuant to this Agreement; provided, however, that (i) the aggregate principal amount of the Debentures shall not exceed $35 million, and (ii) that no Debentures (other than the Debenture instruments evidencing interest payments on the Debentures in accordance with Section 1.1) shall be issued after August 30, 2003 (the "Termination Date"). Upon the execution of the Joinder Agreement appended as Exhibit J hereto by a Purchaser and the Company's issuance of a Debenture to such Purchaser, the conversion

price of the Debentures issued on the Closing Date and the conversion price of any Debenture issued at any time after the Closing Date as provided in this Section 1.2 (b) and Article III hereof, shall be adjusted to give effect to the requirements of Section 1.1(d) hereof, including, without limitation, after giving effect to any change in the number of shares of Common Stock issuable under the Company's outstanding convertible securities (exclusive of the Debentures) as a result of the Company's issuance of additional Debentures following the Closing Date and the application of the anti-dilution provisions contained in the Company's convertible securities.

ARTICLE II

SALE AND PURCHASE OF THE SECURITIES; SECURITY DOCUMENTS

2.1. Sale and Purchase of the Securities. At the Closing, on the terms and subject to the conditions and in reliance on the representations and warranties contained herein, or made pursuant hereto, the Company shall issue, sell and deliver to each Purchaser and such Purchaser's designees, and each Purchaser, severally and not jointly, will purchase from the Company, the Debentures for the purchase prices set forth opposite such Purchaser's name on Exhibit A.

2.2. Company Security Documents. All of the obligations of the Company under the Transaction Documents to or for the benefit of the Purchasers (or their agents and representatives) shall be secured by the following items (collectively, the "Company Debenture Collateral"), each of which, except for Permitted Liens, shall be (i) junior and subordinate to the lien granted to Watson pursuant to the Watson Term Loans, and (ii) senior and superior to those liens granted to the investors in the Existing Debentures, all as more specifically set forth in the Subordination Agreement:

(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 substantially in the form attached as Exhibit E hereto and dated of even date herewith between the Company and Galen Partners III, L.P. ("Galen"), as agent for the Purchasers (such agreement, as supplemented, amended or otherwise modified from time to time in accordance with its terms, the "Company General Security Agreement"), including, without limitation, a lien on and security interest in all of the issued and outstanding shares of common stock of Houba, Inc. and Halsey Pharmaceuticals, Inc. pursuant to a separate Stock Pledge Agreement substantially in the form attached as Exhibit L hereto and dated of even date herewith between the Company and Galen, as agent for the Purchasers (such agreement, as supplemented, amended or otherwise modified from time to time in accordance with its terms, the "Stock Pledge Agreement"):

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

2.3. Guaranties. All of the obligations of the Company under the Debentures shall be guaranteed pursuant to Continuing Unconditional Secured Guaranties substantially in the form of Exhibit F attached hereto (each, a "Guaranty" and collectively, the "Guaranties") by each of the following subsidiaries of the Company (each, a "Guarantor"):

(a) Houba, Inc.; and

(b) Halsey Pharmaceuticals, Inc.

2.4. Guarantor Security Documents. All of the obligations of the Guarantors under the Guaranties shall be secured by the following (collectively, the "Guarantor Debenture Collateral") each of which, except for Permitted Liens, shall be a lien ranking (i) junior and subordinate to the lien granted to Watson pursuant to the Watson Term Loans, and (ii) senior and superior to those liens granted to the investors in the Existing Debentures, all as more specifically set forth in the Subordination Agreement:

(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 Galen, as agent for the Purchasers substantially in the form of Exhibit G attached hereto (such agreement, as supplemented, amended or otherwise modified from time to time in accordance with its terms, the "Guarantors Security Agreement").

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

(c) A mortgage granted by Houba Inc. on real property owned by Houba Inc. 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, L.L.C., 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 referred to as the "Closing Date". The Company and the Purchasers acknowledge and agree that the Debentures may be sold by the Company on one or more Closing Dates. Upon the issuance of additional Debentures under this Agreement, any additional Purchaser (each an "Additional Investor") shall be required to execute a Joinder Agreement in the form attached as Exhibit J hereto (such agreement, as supplemented, amended or otherwise modified from time to time in accordance with its terms, the "Joinder Agreement"), which Joinder Agreement shall include the aggregate principal amount of the Debentures issued to such Purchaser, provided that so long as Care Capital Investments II, LP or Essex Woodlands Health Ventures Fund V (or their respective affiliates (as such term is defined in Rule 501(b) under the Securities Act ("Rule 501(b)")) shall hold Debentures (each such person a "2002 Holder"), the prior written consent of all 2002 Holders shall be required prior to the issuance of any Debentures to any Additional Investors, which consent shall be within their sole and absolute discretion. Any Additional Investors in the Debentures executing a Joinder Agreement shall be deemed a Purchaser for all purposes of this Agreement. Upon the issuance of any Debenture following the Closing Date, the conversion price of the Debentures shall be adjusted as provided in Section 1.2(b) hereof. Notwithstanding anything else contained herein or in the Transaction Documents to the contrary, the Company shall issue no Debentures (other than the Debenture instruments evidencing interest payments on the Debentures in accordance with Section 1.1) after the Termination Date.

On the Closing Date, the Company shall deliver to each Purchaser a Debenture, dated the Closing Date, in the principal amount set forth opposite the name of such Purchaser in Exhibit A. The Company shall deliver the foregoing Debentures against receipt by the Company from each Purchaser of an amount equal to the aggregate purchase price for the Debentures to be purchased by such Purchaser at the Closing, as set forth opposite the name of such Purchaser on Exhibit A, in each case by wire transfer in immediately available funds in U.S. dollars to an account designated by the Company or 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.

ARTICLE IV

REPRESENTATIONS AND WARRANTIES OF THE COMPANY

As a material inducement to each Purchaser to enter into and perform its obligations under this Agreement, except as set forth in the Schedule of Exceptions attached hereto as Exhibit C (the "Schedule of Exceptions"), the Company hereby represents and warrants to you as follows:

4.1. Organization and Existence, etc. The Company is a corporation duly organized, validly existing and in good standing under the laws of New York and is qualified to do business in such other jurisdictions as the nature or conduct of its operations or the ownership of its properties require such qualification. The Company does not own or lease any property or engage in any activity in any jurisdiction that 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 the Purchasers with true, correct and complete copies of its Certificate of Incorporation, By-Laws and all amendments thereto, as of the date hereof.

As used in this Agreement, "Material Adverse Effect" means (a) a material adverse effect on, or change in, the business, prospects, properties, operations, condition (financial or other) or results of operations of the Company and its Subsidiaries, taken as a whole or (b) a material adverse effect on (i) the ability of the Company or any of the Guarantors to perform its respective obligations or (ii) the rights or remedies of any Purchaser under any Transaction Document.

4.2. 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 disclosed in Section 4.2 of the Schedule of Exceptions, all of the outstanding shares of capital stock of each of the Subsidiaries are duly and validly authorized, are validly issued and are fully paid and nonassessable and have been offered, issued, sold and delivered in compliance with applicable Federal and state securities laws. 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 disclosed in Section 4.2 of the Schedule of Exceptions, each Subsidiary is a corporation duly organized, 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 or subject such Subsidiary to a material liability.

4.3. Capitalization. (a) As of the date hereof, the Company's authorized capital stock consists of 80,000,000 shares of Common Stock, par value $.01 per share, of which 15,065,240 shares are outstanding and 66,037,354 shares are reserved for issuance for the purposes set forth in Section 4.3 of the Schedule of Exceptions. Set forth in Section 4.3 of the Schedule of Exceptions is a complete and correct list, as of the date hereof, and as of the Closing Date, of the number of shares of Common Stock held by the Company's public shareholders generally, shareholders holding in excess of 5% of the Company's Common Stock and all holders of options, warrants, debentures and other securities convertible or exercisable for Common Stock. Such schedule is complete and correct in all respects.

(b) All the issued and outstanding shares of capital stock of the Company are (i) duly authorized and validly issued, (ii) 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 of the Schedule of Exceptions there are no outstanding preemptive, conversion or other rights, options, warrants, calls, agreements or commitments granted or issued by or binding upon the Company or any Subsidiary, for the purchase or acquisition of any shares of its capital stock or securities convertible into or exercisable or exchangeable for capital stock.

4.4. Authorization. (a) Each of the Company and the Guarantors has all requisite corporate power and authority (i) to execute and deliver, and to perform and observe their respective obligations under, this Agreement, the Debentures, the Company General Security Agreement, the Stock Pledge Agreement, the Guarantors Security Agreement, the Guaranties, the Mortgage, the Mortgage Subordination Agreement, the Recapitalization Agreement, the Watson Term Loan Amendment, the 2002 Watson Term Loan, the Registration Rights Agreement, the Watson Consent, the Watson Supply Agreement, the Watson Supply Agreement Amendment, the Watson Warrant, the Subscription Agreement with each Purchaser, the Debentureholders Agreement, the Subordination Agreement, the Galen Bridge Lenders Consent, the Existing Debenture Amendments, the Galen Bridge Lenders Consent and the Existing Debentureholder Consent (collectively, the "Transaction Documents") to which it is a respective party, and (ii) to consummate the transactions contemplated hereby and thereby, including, without limitation, the grant of any security interest, mortgage, payment trust, guaranty or other security arrangement by the Company in, on or in respect of the Company Debenture Collateral, and by any and all of the Guarantors in, on or in respect of the Guarantor Debenture Collateral.

(b) All corporate action on the part of (i) the Company and the directors and, except as set forth in Section 4.4(b) of the Schedule of Exceptions or as otherwise provided in Sections 9.7 and 9.12 hereof, the stockholders of the Company necessary for the authorization, execution, delivery and performance by the Company of the Transaction Agreements and the transactions contemplated therein, and for the authorization, issuance and delivery of the Securities, has been taken and (ii) each Guarantor and their respective directors and stockholders

necessary for the authorization, execution, delivery and performance by each Guarantor of the Guarantors General Security Document, the Guaranties and, in the case of Houba, Inc. the Mortgage, and the transactions contemplated therein or in any other Transaction Document with respect to the Guarantors, has been taken.

4.5. Binding Obligations; No Material Adverse Contracts, etc. The Transaction Documents constitute valid and binding obligations of the Company and the Guarantors enforceable in accordance with their respective terms. Except as set forth in Section 4.5 of the Schedule of Exceptions and as provided in Section 9.12 hereof, the execution, delivery and performance by the Company and the Guarantors of the Transaction Documents and compliance therewith 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, or accelerate or permit the acceleration of any rights or obligations, under, any provision of state, local, Federal or foreign law to which the Company or either of the Guarantors is subject, the Certificate of Incorporation, as amended, or the By-Laws, as amended, of the Company or either of the Guarantors, the Watson Term Loans(as amended by the Watson Term Loan Amendment and the Watson Consent, as applicable), the Watson Supply Agreement Amendment, and the Existing Debentures (as amended by the Existing Debentures Amendments and the Existing Debentureholder Consent) or any other mortgage, indenture, agreement, instrument, judgment, decree, order, rule or regulation or other restriction to which the Company or either of the Guarantors is a party or by which it is bound, and except for Permitted Liens, result in the creation of any mortgage, pledge, lien, encumbrance or charge upon any of the properties or assets of the Company or either of the Guarantors pursuant to any such term. Except as set forth in Section 4.3 of the Schedule of Exceptions, no stockholder of the Company or either Guarantor 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.

4.6. Compliance with Instruments, etc. Neither the Company nor any Subsidiary (a) is in violation of its organizational documents, (b) is in default, and no event has occurred which, with the giving of notice, or the lapse of time, or both, would constitute such a default, in the due performance or observance of any term, covenant or condition contained in any material agreement, including, without limitation, the Watson Term Loans, the Watson Supply Agreement, the Watson Supply Agreement Amendment and the Existing Debentures, any license, indenture or other instrument to which it is a party or by which it is bound or to which any of its property or assets is subject or (c) is in violation of any law, ordinance, governmental rule, regulation or court decree to which it or its property may be subject (including without limitation any laws and regulations relating to the biotechnology and pharmaceutical industry) except for such violations under clause (b) and (c) that would not, individually or in the aggregate, have a Material Adverse Effect.

4.7. Litigation. Except as set forth in Section 4.7 of the Schedule of Exceptions, there are no actions, suits or proceedings (including governmental or administrative proceedings), investigations, third-party subpoenas or inquiries by any regulatory agency, body or other governmental authority, to which the Company or any of the Subsidiaries is a party or is subject, or to which any of their authorizations, consents and approvals or other properties or assets, is subject, which is pending, or, to the best knowledge of the Company, threatened or contemplated against the Company or any Subsidiary, or any of such property or assets, that, individually or in the aggregate, could reasonably be expected to have a Material Adverse Effect.

The Company is not subject to any actions, suits or proceedings (including governmental or administrative proceedings), investigation, third-party subpoenas or inquiries by any regulatory agency, body or other governmental authority or any third Person regarding its accounting practices or policies.

4.8. Financial Information; SEC Documents. (a) The Company has furnished to the Purchasers complete and correct copies of the consolidated financial statements of the Company and its Subsidiaries, including consolidated balance sheets as of December 31, 2001 and 2000 and consolidated statements of operations, changes in cash flows and stockholders' equity, covering the three years ended December 31, 2001, all of which statements have been certified by Grant Thornton LLP, independent accountants within the meaning of the Securities Act of 1933, as amended (the "Securities Act") and the rules and regulations thereunder, and all of which statements are included or incorporated by reference in the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2001 filed with the Securities and Exchange Commission (the "Commission") under the Securities Exchange Act of 1934, as amended (the "Exchange Act"). Such financial statements have been prepared in conformity with generally accepted accounting principles in the United States ("US GAAP") applied on a consistent basis throughout the periods involved, except as otherwise stated therein and fairly present the consolidated financial position of the Company and its Subsidiaries as of the dates thereof and their consolidated results of operations for such periods. The Company's auditors have raised no material issues nor delivered any material correspondence with respect to any of the Company's financial statements or financial affairs.

(b) The Company has also furnished to the Purchasers the unaudited consolidated balance sheet of the Company and its Subsidiaries as of September 30, 2002, and the related unaudited consolidated statements of operations, consolidated statements of cash flow and consolidated statements of stockholders' equity for the nine months ended September 30, 2002 and September 30, 2001. Such financial statements were prepared in conformity with US GAAP applied on a basis consistent with the financial statements referred to in paragraph (a) of this Section and fairly present 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 are no facts which the Company has not disclosed to the Purchasers which, individually or in the aggregate, could reasonably be expected to have a Material Adverse Effect.

(d) Except as set forth in Section 4.8 of the Schedule of Exceptions or in the Company's Quarterly Report on Form 10-Q for the quarter ended September 30, 2002, subsequent to December 31, 2001, (i) none of the Company or any Guarantor has incurred any liability or obligations, direct or indirect, or entered into any transactions not in the ordinary course of business, in either case which is material to the Company or any Guarantor, as a whole, (ii) there has not been any material change in the short-term debt or long-term debt of any of the Company or any Guarantor, (iii) there has been no material change in the Company's accounting

principles and (iv) none of the Company or any Guarantor has taken any actions which would have been prohibited under Article X if taken after the date hereof.

(e) Except as set forth in the Company's Quarterly Report on Form 10-Q for the quarter ended September 30, 2002, since December 31, 2001, there has been no Material Adverse Effect with respect to the Company and its Subsidiaries.

4.9. Offering Exemption. (a) None of the Company, its affiliates, as such term is defined in Rule 501(b)) or any Person acting on its or their behalf has engaged or will engage, in connection with the offering and sale of the Securities, in any form in general solicitation or general advertising within the meaning of Rule 502(c) under the Securities Act, and none of the Company, or any of its affiliates, as such term is defined in Rule 501(b) has, directly or indirectly, solicited any offer to buy, sell or offer to sell or otherwise negotiate in respect of, in the United States or to any United States citizen or resident, any security which is or would be integrated with the sale of the Securities in a manner that would require the Securities to be registered under the Securities Act. Assuming the accuracy of the representations and warranties given by the Purchasers in Article V below, the offering, sale and issuance of the Securities have been, are, and will be exempt from registration under the Securities Act, and such offering, sale and issuance is also exempt from registration under applicable state securities and "blue sky" laws.

(b) None of the Company or any Guarantor is, or upon consummation of the transactions contemplated under the Transaction Documents, will be, subject to registration as an "investment company" under the Investment Company Act of 1940, as amended.

4.10. Permits; Governmental and Other Approvals. (a) Other than as set forth in Section 4.10 of the Schedule of Exceptions or in the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2001 or the Company's Quarterly Report on Form 10-Q for the nine months ended September 30, 2002 (collectively, the "Company Reports") each of the Company and its Subsidiaries possesses all necessary consents, approvals, authorizations, orders, registrations, stamps, filings, qualifications, licenses, permits or other analogous acts by, of, from or with all public, regulatory or governmental agencies, bodies and authorities and all other third parties, to own, lease and operate its respective properties and to carry on its business as now conducted and proposed to be conducted except to the extent that the failure to obtain any such consents, approvals, authorizations, orders, registrations, stamps, filings, qualifications, licenses or permits would not have a Material Adverse Effect. Other than as set forth in Section 4.10 of the Schedule of Exceptions, or as otherwise contemplated in Article VI and 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 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 with all applicable provisions of the Federal Food, Drug, and Cosmetic Act (the "FDC Act"), except where any such noncompliance could not reasonably be expected to have a Material Adverse Effect; (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, and will be, in compliance with the following specific requirements: (A) the Company and the Guarantors have registered all of their facilities with the United States Food and Drug Administration (the "FDA"), (B) the Company and the Guarantors have listed their drug products with the FDA, (C) each drug product marketed by the Company or any Guarantor is the subject of an application approved by the FDA, (D) all drug products marketed by the Company or either Guarantor comply with any conditions of approval and the terms of the application submitted to the FDA, (E) all of the Company's and the Guarantors' drug products are manufactured in compliance with the FDA's good manufacturing practice regulations, (F) all of the Company's and the Guarantors' products are labeled and promoted in accordance with the terms of the marketing application and the provisions of the FDC Act, (G) all adverse events relating to the Company and the Guarantors that were required to be reported to the FDA have been reported to the FDA in a timely manner, (H) each of the Company and the Guarantors is in compliance 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, (I) to the Company's best knowledge, neither the Company nor any Guarantor is employing or utilizing the services of any individual who has been debarred under the FDC Act, (J) 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, (K) none of the Company's or a Guarantors' products have been exported for sale outside the United States, and (L) each of the Company and the Guarantors is in compliance with the provisions of the Prescription Drug Marketing Act, to the extent applicable; except, with respect to subclause (iii)(E), (iii)(H), (iii)(G), (iii)(K) and (iii)(L) above, where any such noncompliance could not reasonably be expected to have a Material Adverse Effect.

(c) Without limiting the generality 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 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, except where such noncompliance could not reasonably be expected to have a Material Adverse Effect: (i) 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; (ii) all controlled substances are stored and handled pursuant to DEA security requirements; (iii) all records and inventories of receipt and distributions of controlled substances are maintained in the manner and form as required by DEA regulations; (iv) all reports, including, but not limited to, ARCOS, manufacturing quotas, production quotas, and disposals, have been submitted to the DEA in a timely manner; (v) all adverse events, including thefts or significant losses of controlled substances, have been reported to the DEA in a timely manner; (vi) to the Company's best 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 (vii) any imports or exports of controlled substances have been conducted in compliance with the CSA and DEA regulations.

4.11. Sales Representatives, Customers and Key Employees. (a) To the best knowledge of the Company, no independent sales representatives, customers, officers 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 Guarantor on or after the Closing or in the case of employees, leave, the employ of the Company or any of the Guarantors on and

after the Closing, nor has the Company or any of the Guarantors discussed or taken any steps to terminate the employment of any officer or key employee or group of key employees. Other than as set forth in Section 4.11 of the Schedule of Exceptions, all personnel of the Company and any of the Guarantors are employed on an "at will" basis and may be terminated upon notice of not more than 30 days.

(b) To the Company's best knowledge, no employee of the Company or any of the Guarantors, or any consultant (including any scientific advisor) with whom the Company or any of the Guarantors has contracted, is in violation of any term of any employment contract, proprietary information agreement, licenses, or any other agreement relating to the right of any such individual to be employed by, or to contract with, the Company or any of the Guarantors because of the nature of the business conducted by the Company and the Guarantors; and the continued employment by the Company or any of the Guarantors of their present employees, and the performance of the Company's and the Guarantor's contracts with its independent contractors, will not result in any such violation, except where any such violation could not reasonably be expected to have a Material Adverse Effect. None of the Company or any of the Guarantors has received any written, or to the best knowledge of the Company, oral notice alleging that any such violation has occurred.

(c) All of the Company's and any of the Guarantor's consultants (including scientific advisors), officers and key employees are subject to customary non-disclosure, non-competition and assignment of invention agreements.

4.12. Copyrights, Trademarks and Patents; Licenses. (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, service marks, domain names, 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 best knowledge, 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 Liens, and does not pay, and is not required to pay, any 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, nor has it received any notice relating to, 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.

(e) Except as set forth in Section 4.12 of the Schedule of Exceptions, neither the Company nor any Guarantor is a party to any license agreement pursuant to which the Company is the licensor or licensee of any Intellectual Property Rights.

4.13. Inventory. All inventory of the Company and the Subsidiaries 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 written off or written down to net realizable value on the consolidated balance sheet of the Company and its Subsidiaries as of June 30, 2002. 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.

4.14. Registration Rights. Except as provided for in this Agreement or as set forth in Section 4.14 of the Schedule of Exceptions, 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 under the Securities Act in connection with any sale thereof.

4.15. 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. No charge of discrimination in employment, whether by reason of age, gender, race, religion or other legally protected category that has been asserted or is now pending or, to the best knowledge of the Company and the Guarantors, threatened before the United States Equal Employment Opportunity Commission or other federal or governmental authorities. The Company and each Guarantor is in 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. The Company and each Guarantor has withheld and paid to the appropriate governmental authorities or is holding for payment not yet due to governmental authorities, all amounts required to be withheld from such employees of the Company or the Guarantors and is not liable for any arrears of wages, taxes, penalties or other sums for failure to comply with any of the foregoing. Except as set forth in Section 4.15 of the Schedule of Exceptions, in connection with the operation of the Company's and each Guarantor's business, (a) there is no unfair labor practice charge or complaint against the Company or any Guarantor pending before the National Labor Relations Board or any other governmental agency arising out of the Company's or any Guarantor's activities and the Company has no knowledge, nor has it received notice of any facts or information that would give rise thereto; (b) there is no significant labor trouble, labor strike, material controversy, material unsettled grievance, dispute, request for representation, slowdown or stoppage actually pending against or affecting the Company or any of the Guarantors and, to the best knowledge of the Company, none is or has been threatened; and (c) none of the Company or any of the Guarantors has any collective bargaining agreements with respect to any personnel nor is the Company aware of any current attempts to organize or establish any labor union or employee association with respect to any personnel, nor is there any certification, interim certifications or voluntary recognition of any such union with regard to a bargaining unit.

4.16. Environmental Matters. (a) Without limiting the generality of the representations and warranties given in Section 4.10(a), each of the Company and the Subsidiaries has obtained all environmental, health and safety permits, licenses and other

authorizations 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, and all such permits, licenses and other authorizations are in full force and effect and each of the Company and, except as set forth in Section 4.16 of the Schedule of Exceptions, the Subsidiaries is in compliance with all terms and conditions of such permits, except where such noncompliance could not reasonably be expected to have a Material Adverse Effect.

(b) 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 health or safety permits, licenses or other authorizations necessary for the operation of the business of the Company and the Subsidiaries.

(c) During the occupancy by the Company or any Subsidiary of any real property owned or leased by the Company or such Subsidiary, neither the Company nor any Subsidiary, and to the best knowledge of the Company, no other Person, 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 cleanup, 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 Subsidiary.

(d) Except as set forth in Section 4.16 of the Schedule of Exceptions, neither the Company nor any Subsidiary is subject to any judgment, decree, order or citation related to or arising out of environmental laws, or has received notice that it has been named or listed as a potentially responsible party by any Person in any matter arising under environmental laws.

(e) To the Company's best knowledge, each of the Company and the Subsidiaries has disposed of all waste in full compliance with all environmental laws.

4.17. Taxes. The Company and each of the Guarantors have (a) filed all necessary income, franchise and other material tax returns, domestic and foreign, (b) paid all taxes shown as due thereunder and (c) withheld and paid to the appropriate tax authorities all amounts required to be withheld from wages, salaries and other remuneration to employees. The Company has no knowledge, nor has it received notice, 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.

4.18. 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 their respective ERISA Affiliates are a party or by which the Company, the Guarantors, and any of respective 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 made available to each of the Purchasers: (i) the most recent Plan document and trust agreement (including any amendments thereto and prior plan documents, if amended within 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 (the "PBGC") 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 with applicable law, including but not limited to ERISA, and the Code and with any applicable collective bargaining agreements or other contractual obligations.

(d) 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 Section 412(n) of the Code by reason of a failure of the Company, any Subsidiary, or any ERISA Affiliate to make timely installments or other payments required under Section 412 of the Code.

(e) 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, there are no pending, or to the best knowledge of the Company, its Subsidiaries, and ERISA Affiliates, 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) Except as set forth in Section 4.18 of the Schedule of Exceptions, none of the Company, any Subsidiary, or 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, none of the Company, any Subsidiary or 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) None of the Company, any Subsidiary, or any ERISA Affiliate has engaged, directly or indirectly, in a non-exempt prohibited transaction (as defined in Section 4975 of the Code or Section 406 of ERISA) in connection with any Plan.

(j) No "reportable event" (within the meaning of Section 4043 of ERISA) has occurred with respect to any Plan.

(k) Neither the Company nor any of its Subsidiaries provides, or has provided, retiree welfare benefits for the benefit of any present or former employee or director.

(l) Neither the Company nor any of its Subsidiaries has made any commitment or any formal plan to create any additional Plan or to modify or terminate (except to the extent required by applicable law) any existing Plan.

(m) Neither the Company nor any of its Subsidiaries is a party to any plan, agreement or arrangement pursuant to the terms of which the consummation or announcement of any transaction contemplated by this Agreement will result (either alone or in connection with the occurrence of any additional or further acts or events) in any benefit under any Plan being established or becoming accelerated or immediately vested and payable.

(n) The provisions of Section 280G of the Code will not apply with respect to any payment made or to be made pursuant to or 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 Reports, free and clear of any security interests, options, liens, claims, charges or encumbrances whatsoever, except as set forth in Section 4.19 of the Schedule of Exceptions and as disclosed in the Company General Security Agreement and the Guarantors General Security Agreement. The tangible personal property owned or used by the Company and each of the Guarantors on the date hereof in the operation of its business is adequate for the business conducted by the Company and each of the Guarantors.

4.20. Real Property. (a) The Company and the Guarantors do not own any fee simple interest in real property other than as set forth in Section 4.20 of the Schedule of Exceptions (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 made available to the Purchasers 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 and each Guarantor enjoys a peaceful and undisturbed possession of the Owned Property and Leased Property. No Person other than the Company or any Guarantor 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, 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 subleases, 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. Each Owned Property and Leased Property is used in the conduct of the Company's or the Guarantors' business.

(b) Without limiting the generality of the representations and warranties given in Section 4.10(a), all 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 or Owned 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 in full force and effect, except where the failure to possess such permits, licenses, franchises, approvals and authorizations, individually or in the aggregate, could not reasonably be expected to have a Material Adverse Effect.

(c) 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 the Owned Property or any part thereof.

4.21. Disclosure. The information heretofore provided and to be provided in connection with this Agreement, including, without limitation, the Schedule of Exceptions and the Exhibits hereto, the Transaction Documents and each of the agreements, documents,

certificates and writings previously furnished 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 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 are no facts that (individually or in the aggregate) could reasonably be expected to have a Material Adverse Effect, which has not been set forth herein or in the Company Reports.

4.22. Solvency. On the Closing Date (both before and after giving effect to its Guaranty and the transactions contemplated by the Transaction Documents), Houba, Inc. will be Solvent. As used herein, the term "Solvent" means, with respect to Houba, Inc. on a particular date, that on and as of such date (a) the fair market value of the assets of such Guarantor is greater than the total amount of liabilities (including, without limitations, contingent liabilities) of such Guarantor, (b) the present fair saleable value of the assets of such Guarantor is greater than the amount that will be required to pay the probable liabilities of such Guarantor on its debts as they become absolute and matured, (c) such Guarantor is able to realize upon its assets, through sale, use or borrowing, and is able to pay its debts and other liabilities, including contingent obligations, as they mature and (d) such Guarantor does not have unreasonably small capital.

4.23. Insurance. Each of the Company and the Guarantors maintains, with financially sound and reputable insurers, insurance 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 as well as 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.

4.24 Non-Competes. Except as set forth in Section 4.24 of the Schedule of Exceptions, and as contemplated by Section 4.11(c), the Company and its Subsidiaries are not subject to any non-compete or similar arrangements with any Persons that restrict or may restrict the Company and its Subsidiaries from carrying on its business as now conducted and as it is proposed to be conducted.

4.25 Product Warranty. Except as set forth in Section 4.25 of the Schedule of Exceptions, or as reflected or reserved against in the Financial Statements, (a) to the knowledge of the Company, each product manufactured by the Company or any Subsidiary has been in material conformity with all applicable contractual commitments of the Company or any Subsidiary, and (b) no product currently manufactured by the Company or any Subsidiary is subject to any guaranty, warranty or indemnity of a contractual nature other than the applicable standard terms and conditions, if any, applicable to the sale or delivery of such product.

4.26. Minute Books. The minute books of the Company and the Subsidiaries furnished to the Purchasers for review are accurate and complete.

ARTICLE V

REPRESENTATIONS AND WARRANTIES OF THE PURCHASERS

As a material inducement to the Company to enter into and perform its obligations under this Agreement, each Purchaser severally (as to itself and not with respect to any other Purchaser) 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 any 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 D hereto. Each 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, unless otherwise waived by such Purchaser:

6.1. Representations and Warranties Correct; No Default. The representations and warranties of the Company set forth in Article IV 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. No Event of Default, or any other event which, with the giving of notice, the lapse of time, or both, would constitute an Event of Default, shall have occurred and be continuing on the date of this Agreement or on the Closing Date.

6.2. 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.

6.3. Compliance Certificate. The Company shall have delivered to the Purchaser a certificate of the Company, executed by 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.

6.4. No Impediments. None of the Company, or any of the Guarantors, or any Purchaser shall be subject to (a) any order, decree or injunction of a court or administrative or governmental body or agency of competent jurisdiction directing that the transactions provided for in the Transaction Documents or any material aspect thereof not be consummated as contemplated by the Transaction Documents or (b) there shall not be any action, suit, proceeding, complaint, charge, hearing, inquiry or investigation before or by any court or administrative or governmental body or agency pending or, to the Company's best knowledge, threatened, wherein an unfavorable order, decree or injunction would prevent the performance of

any of the Transaction Documents or the consummation of any material aspect of the transactions or events contemplated thereby, declare unlawful any aspect of the transactions or events contemplated by the Transaction Documents, cause any material aspect of the transactions contemplated by the Transaction Documents to be rescinded or have a Material Adverse Effect.

6.5. Waivers/Elections of Rights of First Refusal. The Company shall have obtained from each Person other than a Purchaser and 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.

6.6. Watson Consent; Amendment to Watson Term Loans; Subordination Agreement. The Company shall have obtained (a) the consent of Watson to the consummation of the transactions contemplated by the Transaction Agreements, including, without limitation, the issuance of the Securities, the incurrence of the Indebtedness evidenced by the Debentures and the grant of the liens covering the assets of the Company and the Guarantors in favor of the Purchasers as provided herein, which consent shall be in form and substance reasonably acceptable to the Purchasers (the "Watson Consent"); (b) an amendment to the loan documents evidencing the 2000 Watson Term Loan, duly executed by the Company, the Guarantors and Watson, providing for (i) the extension of the maturity date of the Watson Term Loan from March 31, 2003 to March 31, 2006, (ii) the Company's issuance of the Watson Warrant exercisable for 10,700,665 shares of Common Stock, which amendments to the Watson Term Loan shall be in form and substance reasonably acceptable to the Purchasers and (iii) the issuance of a new term consent to the issuance of a new term loan to the Company by Watson to take into account the excess payments made by Watson to the Company of approximately $3,901,331 (the "2002 Watson Term Loan") (the "Watson Term Loan Amendment"); (c) consent to the issuance of the 2002 Watson Term Loan pursuant to the Watson Term Loan Amendment and the Watson Supply Agreement in form and substance reasonably acceptable to the Purchasers (the "Watson Supply Agreement Amendment"); and (d) a Subordination Agreement substantially in the form attached hereto as Exhibit M by and among the Company, Watson, the Purchasers, the holders of the Existing Debentures and certain other parties signatory thereto (such agreement, as supplemented, amended or otherwise modified from time to time in accordance with its terms, the "Subordination Agreement") confirming, among other things, their relative rights with respect to the Company Debenture Collateral and the Guarantors Debenture Collateral, respectively.

6.7. Consent of Holders of Existing Debentures. The Company shall have obtained (a) the consent of the holders of the Existing Debentures to waive the Indebtedness, lien, registration rights, and charter amendment restrictions contained in each of the Debenture and Warrant Purchase Agreements pursuant to which the Existing Debentures were issued (the "Existing Debentureholders Consent"); (b) an amendment to each of the Debenture and Warrant Purchase Agreements pursuant to which the Existing Debentures were issued, duly executed by the Company and each holder of the Existing Debentures, providing for (i) the extension of the maturity date of the Existing Debentures from March 15, 2003 to March 31, 2006, and (ii) the exercise of any preemptive rights granted to the holders of the Existing Debentures on a pro rata basis with the Purchasers of the Debentures under this Agreement (the "Existing Debenture Amendments"); (c) the Subordination Agreement and; (d) the Debenture Dilution Waiver. Each of the Existing Debentureholders Consent and the Existing Debenture Amendments shall be in form and substance reasonably acceptable to the Purchasers.

6.8. Consent of Galen Bridge Lenders. The Company shall have (a) obtained from the Galen Bridge Lenders the consent to surrender and convert the Galen Bridge Notes in exchange for and into Debentures in form and substance reasonably acceptable to the Purchasers (the "Galen Bridge Lenders Consent"), and (b) prepaid any Galen Bridge Notes not so surrendered and converted in accordance with their terms and the terms of the Galen Bridge Loan Agreement (other than Galen Bridge Notes held by Galen, which must be converted in accordance with subsection 6.8(a)).

6.9. Recapitalization Agreement. The Company shall have executed the Recapitalization Agreement in substantially the form of Exhibit N hereto (the "Recapitalization Agreement") and shall have caused each of the holders of the Company's Common Stock purchase warrants listed on the signature page thereto (the "Warrant Holders") to have executed the Recapitalization Agreement, providing for the Warrant Holders surrender to the Company of the common stock purchase warrants described in Schedule A to the Recapitalization Agreement in exchange for an aggregate of approximately 5,970,083 shares of the Company's Common Stock and the transaction contemplated thereby shall have been consummated.

6.10. Other Agreements and Documents. The Company shall have executed and delivered to each Purchaser this Agreement, issued to such Purchaser all of the Securities and the Company and each of the Guarantors, as applicable, shall have executed and delivered the following agreements and documents:

(a) The Company General Security Agreement;

(b) The Guaranties;

(c) The Guarantors Security Agreement;

(d) The Stock Pledge Agreement;

(e) Financing Statements and Termination Statements on Form UCC-1 and Form UCC-3 (or the applicable form), respectively, with respect to all personal property and assets of the Company and each Guarantor;

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

(g) Resolutions by the Board of Directors of each of the Company and the Guarantors approving the execution, delivery and performance of this Agreement and the other Transaction Documents and the transactions contemplated hereby and thereby;

(h) 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;

(i) 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;

(j) The Mortgage;

(k) The Mortgage Subordination Agreement;

(l) The Watson Consent;

(m) The Watson Term Loan Amendment;

(n) The 2002 Watson Term Loan

(o) The Watson Supply Agreement Amendment;

(p) The Subordination Agreement;

(q) The Watson Warrant;

(r) The Registration Rights Agreement;

(s) The Galen Bridge Lenders Consent;

(t) The Existing Debentureholders Consent;

(u) The Existing Debenture Amendments;

(v) The Debentureholders Agreement;

(w) The Subscription Agreement with each Purchaser

(x) The Voting Agreement; and

(y) The Recapitalization Agreement.

6.11. Consents. In addition to the consents described in Section 6.6, 6.7 and 6.8, the Company shall have obtained all necessary consents or waivers, if any, from all parties governmental and private 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 by the Transaction Agreements may be consummated and the business of the Company may be conducted by the Company after the Closing without adversely affecting the Company.

6.12. Legal Investment. As of the Closing Date, there shall not have been any change in any law, statute, ordinance, rule, code, approvals, governmental restriction, regulation, permit, order, writ, injunction, judgment or decree, applicable to any of the Purchasers that would prevent the performance of this Agreement or any other Transaction Document or the consummation of any material aspect of the transactions contemplated hereby or thereby by such Purchaser, in each case to the extent that it would deprive such Purchaser of the principal benefits of such transactions.

6.13. Proceedings and Other Documents. All corporate and other proceedings taken or required to be taken by the Company and any Guarantor in connection with the transactions contemplated by this Agreement and the other Transaction Documents to be

consummated prior to the Closing shall have been taken, except as otherwise provided in Sections 9.7 and 9.12 hereof, 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 transactions contemplated hereby as the Purchasers may reasonably request.

6.14. 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 H attached hereto.

6.15. Reconstitution of the Board of Directors. The Board of Directors of the Company shall have been reconstituted to consist of 11 members, comprised as follows: (a) one member, who shall be a designee of Care Capital Investments II, LP, (b) one member, who shall be a designee of Essex Woodlands Health Ventures Fund V, (c) up to two members, who shall be executive officers of the Company, (d) three members, who shall be designees of the holders of the March 1998 Debentures, (e) one member, who shall be a designee of the holders of the May 1999 Debentures, and (f) three members (increased to the extent of any reduction in the number of Board member also serving as executive officers of the Company), who shall be independent directors nominated and elected to the Board by the then current board members, subject to the consent to the appointment and election of such independent Board members by each Board member who is a designee of Care Capital Investments II, LP or Essex Woodlands Health Ventures Fund V. The Company shall have provided the Purchasers with the resignation of such members of the Company's current Board of Directors so as to reconstitute the Board of Directors as provided in this Section 6.15. Notwithstanding the foregoing, the designees of the holders of the March 1998 Debentures to the Board of Directors shall be reduced from three to two commencing as of and following the second Annual Meeting of the Company's shareholders which occurs following the date of this Agreement.

6.16. Authorized Shares. The Company shall have received from each of Galen, Galen Partners International III, L.P., Galen Employee Fund III, L.P. and Oracle Strategic Partners, L.P. (collectively, the "Institutional Existing Debentureholders") a written consent authorizing the Company to release, on a pro rata basis, (a) from its authorized but unissued reserved shares of Common Stock such number of shares of Common Stock, otherwise reserved for the Institutional Existing Debentureholders (the "Institutional Existing Debentureholders Reserved Shares"), as are necessary to permit the conversion at any time on or after the Closing of all of the Debentures purchased hereunder by each of Care Capital Investments II, LP and Essex Woodlands Health Ventures Fund V, and (b) from the Institutional Existing Debentureholders Reserved Shares such number of additional shares of Common Stock as necessary to be reserved to take into account any change in the Conversion Price (as defined in the Debenture) of the Debentures purchased hereunder by each of Care Capital Investments II, LP and Essex Woodlands Health Ventures Fund V.

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, unless otherwise waived by the Company:

7.1. Representations. The representations and warranties of each of the Purchasers set forth in Article V hereof and in the Subscription Agreement 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.

7.2. Legal Investment. As of the Closing Date, there shall not have been any change in any law, statute, ordinance, rule, code, approvals, governmental restriction, regulation, permit, order, writ, injunction, judgment or decree, applicable to the Company that would prevent the performance of this Agreement or any other Transaction Document or the consummation of any material aspect of the transactions contemplated hereby or thereby by the Company, in each case to the extent that it would deprive the Company of the principal benefits of such transactions.

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

ARTICLE VIII

PREPAYMENT

No Optional Prepayments. Without limiting the Company's conversion rights as provided in Section 3.2 of the Debentures, the Company may not at any time, without the prior written consent of the holders of all of the holders of the outstanding Debentures, prepay any Debenture, the Watson Term Loans, the Existing Debentures or any other indebtedness existing now or hereafter, in whole or in part.

ARTICLE IX

AFFIRMATIVE COVENANTS

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

9.1. Maintenance of Corporate Existence, Properties and Leases; Taxes; Insurance. 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 terms of licenses and other rights to use licenses, trademarks, trade names, service marks, copyrights, patents, processes or any other Intellectual Property Rights owned or possessed by it and necessary to the conduct of its business, except where failure to maintain such rights, franchises and terms of licenses and other

rights to use such Intellectual Property Rights could not reasonably be expected to have a Material Adverse Effect.

(a) 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 provision of all leases to which it is a party or under which it occupies property, except where any such noncompliance could not reasonably be expected to have a Material Adverse Effect.

(b) The Company shall and shall cause each of the Guarantors to (i) 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, (ii) withhold and promptly pay to the appropriate tax authorities all amounts required to be withheld from wages, salaries and other remuneration to employees, and (iii) promptly pay 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 (i) the validity thereof shall be contested timely and in good faith by appropriate proceedings, (ii) the Company or the Guarantors shall have set aside on its books adequate reserves with respect thereto, and (iii) 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.

(c) 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.

9.2. 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 30 days after the end of each of the 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 US GAAP consistently applied, and will fairly present the consolidated financial position of the Company and its Subsidiaries as of the dates thereof and their consolidated results of operations for such periods;

(b) within 90 days after the end of each fiscal year (or within five days after being filed with the Commission, if sooner), 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 US GAAP, consistently applied, and will fairly present the consolidated financial position of the Company and its Subsidiaries as of the dates thereof and their consolidated results of operations for such periods, and will be accompanied by:

(i) a 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 an Event of Default has occurred with respect to this Agreement or the Debentures or, if such accountants have reason to believe that any such Event of Default has occurred, a letter specifying the nature thereof; and

(iii) the management letter of such accounting firm;

(c) within 45 days after the end of each quarterly accounting period in each fiscal year (or within five days after being filed with the Commission, if sooner) consolidated statements of income and retained earnings and cash flows of the Company and its Subsidiaries for such quarterly accounting period and for the period from the beginning of each fiscal year to the end of such quarterly accounting period and consolidated balance sheets as at the end of such quarterly accounting period, setting forth in each case in comparative form corresponding figures for the preceding quarterly accounting period, which statements will be prepared in accordance with US GAAP, consistently applied, and will fairly represent the consolidated financial position of the Company and its Subsidiaries as of the dates thereof and their consolidated results of operations for such periods;

(d) within 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 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 90 days after the end of the fiscal year;

(e) promptly upon receipt thereof, but in no event later than three business days, 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;

(f) at least 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;

(g) within ten 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"), the National Association of Securities Dealers Automated Quotation System ("NASDAQ") or with any other securities exchange or over-the-counter market on which any of the securities of the Company are then listed or approved for trading, 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

(h) 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. Notwithstanding the foregoing, all confidential information furnished at any time by or on behalf of the Company or its Subsidiaries to any Purchaser (or any transferee of any Securities) shall be subject to the provisions of Section 19.13.

9.3. Notice of Adverse Change. The Company shall promptly give notice to all holders of any Securities (but in any event within two 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 or any default that with the passage of time or the giving of notice would constitute an Event of Default;

(b) the institution or threatening of institution of any 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 reasonably be expected to have a Material Adverse Effect;

(c) any information relating to the Company or any Subsidiary which could reasonably be expected to have a Material Adverse Effect; or

(d) any failure by the Company or any of its Subsidiaries to comply with the provisions of Section 9.4 below.

Any notice given under this Section 9.3 shall specify the nature and period of existence of the condition, event, information, development or circumstance, the anticipated effect thereof and what actions the Company or any Guarantor, as the case may be, has taken and proposes to take with respect thereto.

9.4. 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 with any 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, in each case except for any such noncompliance that could not reasonably be expected to have a Material Adverse Effect.

9.5. 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 or Intellectual Property Rights 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.

9.6. 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 US GAAP applied on a consistent basis.

(b) The Company (subject to the terms and conditions contained in Section 19.13) 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 to make extracts or copies of the books, accounts and records of the Company or its Subsidiaries, and 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 that a holder of any Securities 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.

(d) The Company will retain a firm of independent certified public accountants reasonably acceptable to the Purchasers (an "Approved Accounting Firm") to audit the Company's financial statements at the end of each fiscal year. In the event the services of an Approved Accounting Firm or any firm of independent public accountants hereafter employed by the Company are terminated, the Company will promptly thereafter request the firm of independent public accountants whose services are terminated to deliver to the Purchasers a letter of such firm setting forth its understanding as to the reasons for the termination of their services and whether there were, during the two most recent fiscal years or such shorter period during which said firm had been retained by the Company any disagreements between them and the Company on any matter of accounting principles or practices, financial statement disclosure, or auditing scope or procedure. In its notice, the Company shall state whether the change of accountants was recommended or approved by the Board of Directors or any committee thereof. In the event of such termination, the Company will promptly thereafter engage another Approved Accounting Firm.

9.7. Board Members and Meetings. (a) So long as the Purchasers own any Debentures, the Board of Directors of the Company shall be comprised of 11 members. The Company agrees to hold meetings of its Board of Directors at least four times a year, at no more than three month intervals. So long as the Purchasers own any Debentures, Care Capital Investments II, LP shall have the right to designate for nomination one person, and Essex Woodlands Health Ventures Fund V shall have the right to designate for nomination one person (collectively, the "Designees"), to be members of the Company's Board of Directors and the Company shall cause (i) such Designees to be elected to the Board of Directors on the Closing Date, (ii) such Designees to be nominated for election at each Annual Meeting of Shareholders of the Company, and at each special meeting of the shareholders of the Company called for the purpose of electing directors of the Company and at any time at which the shareholders of the Company have the right to elect directors of the Company, and shall recommend that the Company's shareholders vote in favor of the election of such nominees, and (iii) such Designees shall be, if so requested by such Designee in its sole discretion, appointed to the Company's Executive Committee, Compensation Committee and any other committee of the Company. So long as the Purchasers own any Debentures, at each Annual Meeting of the Shareholders of the

Company held thereafter, the Designees shall be, if so requested by such Designee in its sole discretion, appointed to the Company's Executive Committee and Compensation Committee and any other committee of the Company. Directors shall be reimbursed for their reasonable travel and related expenses in attending Board meetings.

(b) In lieu of having its Designee nominated for election as a director of the Company as set forth above, each of Care Capital Investments II, LP and Essex Woodlands Health Ventures Fund V may, at its election and upon written notice to the Company, appoint a nonvoting "observer", who shall (i) be provided by the Company with all notices of meetings, consents, minutes and other materials that are provided to the Board of Directors (or any committee thereof) at the same time as such materials are provided to the Board of Directors (or any committees thereof) and (ii) be entitled to attend all meetings of the Board of Directors, including all meetings of the Company's Executive Committee, Audit Committee and Compensation Committee and any other committee of the Company; provided, however, that any such information provided to a nonvoting "observer" shall be subject to the provisions of Section 19.13.

(c) So long as the Purchasers own any Debentures, each of Care Capital Investments II, LP and Essex Woodlands Health Ventures shall have the right to have a representative join the Company's Scientific Advisory Board, subject to the approval of the Company's Board of Directors and subject further to the provisions of Section 19.13.

9.8. Maintenance of Office. The Company will maintain its principal office at the address of the Company set forth in Section 19.5 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 30 days prior thereto, of any change of location of such office.

9.9. Use of Proceeds. The Company shall use all the proceeds received from the sale of the Securities pursuant to this Agreement for general working capital.

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

9.11. 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 any Securities promptly upon filing with the Commission.

9.12. Amendments to the Company's Certificate of Incorporation. (a) The Company will present to its shareholders and debentureholders for consideration at the Company's next 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 80,000,000 to such number of shares as shall equal

the sum of (A) the Company's issued and outstanding Common Stock, plus (B) the number of shares of Common Stock issuable upon the conversion and exercise of the Company's outstanding convertible securities, plus (C) the number of shares of Common Stock issuable upon conversion of the Debentures and exercise of the Watson Warrant, plus (D) 50 million shares, as shall sum shall be rounded up to the nearest whole five million shares; (ii) a proposal to amend the Company's Certificate of Incorporation to provide that holders of the 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 the holders of the Debentures 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, provided, however, that any Debentures held by Care Capital Investments II, LP shall, for so long as they are held by Care Capital Investments II, LP, have no such voting rights and the Certificate of Incorporation and the Debentures shall so state; and (iii) a proposal to elect as directors one Designee of each of Care Capital Investments II, LP and Essex Woodlands Health Ventures Fund V, which Designees shall also be appointed, if so requested by such Designee in its sole discretion, to the Company's Executive Committee and Compensation Committee and any other committee of the Company,. Upon receipt of shareholder approval of any such charter amendments, the Company will promptly file such amendment to its Certificate of Incorporation with the Secretary of State of the State of New York.

(b) Each of Galen, Galen Partners International III, L.P., Galen Employee Fund III, L.P., Oracle Strategic Partners, L.P., Michael Reicher Trust, Robert W. Baird & Co., Inc., TTEE FBO Michael K. Reicher IRA, trusts created for the benefit of Michael K. Reicher, the Company's Chairman and Chief Executive Officer and Peter Clemens, the Company's Chief Financial Officer, as investors in the Existing Debentures, has executed and delivered a Voting Agreement in substantially the form attached hereto as Exhibit I (such agreement, as supplemented, amended or otherwise modified from time to time in accordance with its terms, the "Voting Agreement") providing that, among other things, each such Person shall vote the shares of the Company's Common Stock (including shares underlying the Existing Debentures) owned by it in favor of the proposals described in Section 9.12(a) above. Each of Galen, Galen Partners International III, L.P., Galen Employee Fund III, L.P., Oracle Strategic Partners, L.P., Michael Reicher and Peter Clemens severally represents and warrants that such Voting Agreement has been duly authorized, executed and delivered by such Person and is such Person's legal, valid and binding agreement, enforceable against it in accordance with its terms.

Notwithstanding anything to the contrary contained herein, (i) the Company will use its best efforts to cause the approvals and amendments provided herein to be obtained in accordance with the terms hereof and otherwise as soon as reasonably possible, and (ii) the Board of Directors will recommend to the Company's shareholders and debentureholders the approval of the amendments to the Company's Certificate of Incorporation as provided in this Section 9.12.

9.13. Director and Officer Insurance Coverage. As soon as practicable, but in any event within 30 days following the Closing, the Company shall obtain "directors and officers" insurance ("D&O Insurance") mutually acceptable to the Purchasers and the Company covering those persons who are directors and officers of the Company, which D&O Insurance shall provide at least a minimum of $5,000,000 of coverage per director. The Company shall maintain

a such D&O Insurance covering its directors and officers with financially sound and reputable insurers insuring the Company's directors and officers from the liability and expense customarily insured under such "director and officer" insurance policies.

9.14. 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 the transactions contemplated hereby 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 66 2/3% in aggregate principal amount of the Debentures then outstanding, as follows:

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

10.2. Reclassification. Effect any reclassification, combination or reverse stock split of the Common Stock of the Company.

10.3. Liens. Except as otherwise provided in this Agreement or any other Transaction Document, 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 US GAAP consistently applied shall have been made therefor;

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

(c) liens securing Indebtedness of the Company or any Subsidiary which are permitted under Section 10.4(b) or (g);

(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 reserves or other appropriate provisions, if any, as shall be required by US GAAP, shall have been made for any such contested amounts;

(e) liens incurred or deposits made in the ordinary course of business in connection with workers' compensation, unemployment insurance and other types of social security, or to secure the performance of tenders, statutory obligations, surety and appeal bonds, bids, leases, government contracts, trade contracts, performance and return-of-money bonds and other similar obligations (exclusive of obligations for the payment of borrowed money);

(f) any attachment or judgment lien not otherwise constituting an Event of Default, or an event which, with the giving of notice, the lapse of time, or both, would not otherwise constitute 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 with the ordinary conduct of the business of the Company or any of its Subsidiaries, except where such interference could not reasonably be expected to have a Material Adverse Effect;

(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 Indebtedness 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 10.3(l) of the Schedule of Exceptions ("Permitted Liens"); and

(m) the replacement, extension or renewal of any lien permitted by this Section 10.3 upon or in the same property theretofore subject or the replacement, extension or renewal (without increase in the amount or change in any direct or contingent obligor) of the Indebtedness secured thereby.

10.4. Indebtedness. Create, incur, assume, suffer, permit to exist, or guarantee, directly or indirectly, any Indebtedness, excluding:

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

(b) 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 on terms reasonably satisfactory to the Purchasers;

(c) Indebtedness existing on the date hereof and described in Section 10.4 of the Schedule of Exceptions;

(d) 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;

(e) Indebtedness relating to loans from the Company to its Subsidiaries or Indebtedness owed to any of the Guarantors;

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

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

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

(i) The Debentures.

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 (but also shall include any "off-balance sheet financings") 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 in good faith by the Company or a Subsidiary, as applicable), 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 a Subsidiary) for which the Company (or a Subsidiary) is obligated, contingently or otherwise, to purchase or otherwise acquire, or for the payment or purchase of which the Company (or a Subsidiary) has agreed, contingently or otherwise, to advance or supply funds, or with respect to

which the Company (or a Subsidiary) is contingently liable, including, without limitation, indebtedness for borrowed money and indebtedness guaranteed or supported indirectly by the Company (or a Subsidiary) through an agreement, contingent or otherwise (x) to purchase the indebtedness, or (y) 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 (z) 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 any of its consolidated Subsidiaries.

10.5. 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.

10.6. Immaterial Subsidiaries. The Company shall not permit any of the Immaterial Subsidiaries to commence any business operations of a type or scope not currently conducted by them, nor permit any Immaterial Subsidiary to acquire any rights or property not currently owned by it.

10.7. Loans and Advances. Except for loans and advances outstanding as of the Closing Date and set forth in Section 10.7 of the Schedule of Exceptions, directly or indirectly, make any advance or loan to, or guarantee any obligation of, any person, firm or entity, except for intercompany loans or advances in the ordinary course of business and those provided for in this Agreement. The Company and the Guarantors shall comply in all material respects with the requirements of the Sarbanes-Oxley Act of 2002, and the rules and regulations promulgated thereunder, as amended from time to time.

10.8. Intercompany Transfers; Transactions With Affiliates; Diversion of Corporate Opportunities. (a) Make any intercompany transfers of monies or other assets in any single transaction or series of transactions, except as otherwise permitted in this Agreement.

(b) Engage in any transaction with any of the officers, directors, employees or "affiliates" (as such term is defined in Rule 501(b)) of the Company or of its Subsidiaries, except on terms no less favorable to the Company or the Subsidiary as could be obtained at Arm's Length.

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

10.9. Investments. Make any investments in, or purchase any stock, option, warrant, or other security or evidence of Indebtedness of, any Person (exclusive of any Subsidiary), other than obligations of the United States Government or certificates of deposit or

other instruments maturing within one year from the date of purchase from financial institutions with capital in excess of $100 million.

10.10. Other Business. Enter into or engage, directly or indirectly, in any business other than the business currently conducted or proposed to be conducted as disclosed to the Purchasers prior to the date hereof by the Company or any Subsidiary.

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

(a) enter into or materially amend any agreement to provide for or otherwise establish any written or unwritten employee benefit plan, program or other arrangement of any kind, covering current or former employees of the Company or its Subsidiaries except for any such plan, program or arrangement expressly permitted under an existing agreement listed in Section 4.18 the Schedule of Exceptions; provided, however, that no such plan, program or arrangement may be established or implemented if such action would have a material effect on the terms of employment of the employees of the Company or its Subsidiaries; or

(b) provide for or agree to any material increase in any benefit provided to current or former employees of the Company or its Subsidiaries over that which is provided to such individuals pursuant to a plan or arrangement disclosed in Section 4.18 of the Schedule of Exceptions as of the Closing Date; or

(c) provide for or agree to any increase in the annual compensation of any of the employees of the Company or its Subsidiaries, except for (i) annual salary increases in the ordinary cause of business consistent with past practice (not to exceed a 10% increase over such employee's annual salary compensation on the date hereof), and (ii) normal and customary annual bonuses to employees (not to exceed $350,000 in the aggregate in any fiscal year in the absence of the approval of the Board of Directors).

10.12. Capital Expenditures. Other than for capital expenditures contained in any budget approved by the Board of Directors, make or commit to make, or permit any of its Subsidiaries to make or commit to make, any capital expenditures in excess of $250,000 in the aggregate during any fiscal year of the Company.

10.13. Amendment, Etc. of Certain Document. Except as otherwise specifically provided for herein, amend, modify, change in any manner any term or condition of the Watson Term Loans, the Existing Debentures or any agreement or other instrument or document entered into by the Company or any Guarantor in connection therewith or pursuant thereto, or give any consent, waiver or approval thereunder, waive any default under or any breach of any term or condition thereof, agree in any manner to any other amendment, modification or change of any term or condition thereof or take any other action in connection therewith that would impair the value of the interest or the rights of any Purchaser under this Agreement or any other Transaction Document, or permit any of the Guarantors to do any of the foregoing without the prior written consent of all the Purchasers.

10.14. Formation of Subsidiaries. Organize or invest, or permit any Subsidiary to organize or invest, in any new corporation, partnership, joint venture, limited liability company, trust or estate of which (or in which) (a) more than 50% of the issued and outstanding capital stock having ordinary voting power to elect a majority of the board of directors of such corporation (irrespective of whether at the time capital stock of any other class of such corporation shall or might have voting power upon the occurrence of any contingency), the interest in the capital or profits of such partnership, joint venture or limited liability company or the beneficial interest in such trust or estate, is at the time directly or indirectly owned or controlled by the Company, any of its Subsidiaries or any of their respective officers or directors, or (b) a material minority investment in any such entity is directly or indirectly owned or controlled by the Company, any of its Subsidiaries or any of their respective officers or directors.

10.15 Prohibition on Certain Cash Interest Payments. The Company shall not make any cash interest payments to Galen, Galen Partners International III, L.P., Galen Employee Fund III, L.P. or Oracle Strategic Partners, L.P., pursuant to the March 1998 Debentures or the May 1999 Debentures, notwithstanding anything else to the contrary contained therein or elsewhere, without the prior written consent of all 2002 Holders, which consent shall be within their sole and absolute discretion.

ARTICLE XI

INTENTIONALLY OMITTED

ARTICLE XII

EVENTS OF DEFAULT

12.1. Events of Default. If any of the following events shall occur and be continuing on or before the Security Interest Termination Date, 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 (including, without limitation, the principal of any Interest Payment 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 (including, without limitation, interest on any Interest Payment Debentures), when the same shall become due and payable, and in the case of an interest payment such default shall have continued without cure for ten days from the scheduled date of payment of such interest;

(b) the Company shall fail to issue to a Holder the Shares issuable upon conversion of a Debenture pursuant to the instructions provided by such Holder and in accordance with the terms of such Debenture;

(c) except or provided in Section 12.1(b), if the Company shall default in the performance of any of the covenants contained in Articles IX or X, and, in the case of a default under Sections 9.1 through and including 9.8 or Section 10.3 (exclusive of Section 10.3(c)), such default shall have continued without cure for 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 (and the Company shall give to all other holders of the Debentures at the time outstanding prompt written notice of the receipt of such Default Notice, specifying the default referred to therein); provided, however, that such 30-day grace period shall not apply in the event the Company fails to promptly give notice as provided in Section 9.3;

(d) except as provided in Sections 12.1(b) or 12.1(c), if the Company or any of the Guarantors shall default in the performance of any other agreement contained in any Transaction Document or in any other agreement executed in connection with this Agreement and such default shall not have been remedied to the satisfaction of the holders of 66 2/3% in aggregate principal amount of the Debentures then outstanding, within 45 days after a Default Notice shall have been given to the Company (and the Company shall give to all other holders of Debentures at the time outstanding prompt written notice of the receipt of such Default Notice, specifying the default referred to therein) provided, however, that such thirty-five (35) day grace period shall not apply in the event the Company fails to give notice as provided in Section 9.3;

(e) if any representation or warranty made by the Company, any Guarantor or any of their officers in any Transaction Document or in or any certificate delivered pursuant thereto shall prove to have been incorrect when made;

(f) if (i) 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 (or being declared by its holders or, on its behalf, by an agent or trustee therefor to be) due and payable prior to its due date; or (ii) irrespective of the monetary thresholds specified in subclause (i) above, any default, event of default or any other condition shall occur or exist under the Watson Term Loans or any Existing Debentures (as such term is defined in the Watson Term Loan and the Existing Debentures, respectively) which shall be continuing after the respective grace period, if any, specified in the Watson Term Loans and the Existing Debentures, and the effect of which is to accelerate, or to permit the acceleration of, the maturity of the Indebtedness outstanding thereunder; or (iii) a Change of Control shall have occurred;

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

(h) if the Company shall fail to obtain from the DEA a raw material import registration authorizing the Company to import raw poppy for use in the Company's manufacturing operations, on or before December 31, 2004;

(i) if the Watson Supply Agreement shall have been terminated in accordance with its terms and the Company fails, within a period of 60 days from the effective date of such termination, to secure alternative supply and distribution arrangements with third

parties or to commence the marketing and sale of the products that are the subject of such agreement (each an "Alternative Arrangement"), which Alternative Arrangements are reasonably expected to generate revenues during the 12-month period commencing with the start of such Alternative Arrangements of not less than 70% of the revenues derived form the Core Products Agreement for the fiscal year immediately preceding the termination of the Core Products Agreement;

(j) if a final judgment which, either alone or together with other outstanding final judgments against the Company and its Subsidiaries, exceeds an aggregate of $750,000 shall be rendered against the Company or any Subsidiary and such judgment shall have continued undischarged or unstayed for 60 days after entry thereof;

(k) if the Company or any Subsidiary shall generally not pay its debts as such debts become due or shall make an assignment for the benefit of creditors generally, or shall admit in writing its inability to pay its debts generally; or if any proceeding shall be instituted by or against the Company or any Subsidiary seeking to adjudicate it as bankrupt or insolvent, or seeking liquidation, winding up, reorganization, arrangement, adjustment, protection, relief or composition of it or its debts under any law relating to bankruptcy, insolvency or the reorganization or relief of debtors, or seeking entry of an order for relief or the appointment of a receiver, trustee, custodian or other similar official for it or for any substantial part of its property and, in the case of such proceeding instituted against it (but not instituted by it) that is being diligently contested by it in good faith, either such proceeding shall remain undismissed or unstayed for a period of 90 days or any of the actions sought in such proceeding (including, without limitation, the entry of an order for relief against, or the appointment of a receiver, trustee, custodian or other similar official for, it or any substantial part of its property) shall occur; or if any writ of attachment or execution or any similar process shall be issued or levied against it or any substantial part of its property which is either not released, stayed, bonded or vacated within 90 days after its issue or levy or any of the actions sought or relief sought in any proceeding pursuant to which such writ or similar process shall be issued or initiated shall occur or be granted; or if the Company or any Subsidiary takes corporate action in furtherance of any of the aforesaid purposes or conditions;

(l) if any provision of any Transaction Document shall for any reason cease to be valid and binding on, or enforceable against, the Company or any Guarantor, or the Company or any Guarantor shall so assert in writing; or

(m) any Transaction Document (or any financing statement) which purports:

(i) to create, perfect or evidence a lien on or security interest in any Company Debenture Collateral or Guarantor Debenture Collateral in favor of the Purchasers (or their agents and representatives), or to provide for the priority of any such lien or security interest over the interest of any other party in the same Collateral, shall cease to create, or to preserve the enforceability, perfection or first priority (subject to the Subordination Agreement and, if applicable, the Mortgage Subordination Agreement) of, such lien and security interest; or

(ii) to provide for the priority in right of payment of the Company's obligations under the Transaction Documents to or in favor of the Purchasers (or their agents or representatives) shall cease to preserve such priority.

12.2. Remedies. (a) Except as provided in Section 12.2(b) or (c) hereof, upon the occurrence and during the continuance of an Event of Default, any holder or holders of 66 2/3% 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 by the Company; and (ii) declare any other amounts payable to the Purchasers under this Agreement or as contemplated hereby due and payable; provided, however, that in the event of an actual or deemed entry of an order for relief with respect to the Company under the Federal Bankruptcy Code, the Debentures, together with interest accrued thereon, shall automatically become and be due and payable, without presentment, demand, protest or notice of any kind, all of which are hereby waived by the Company.

(b) Notwithstanding anything to the contrary 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 66 2/3% 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 in Section 12.2(a), upon the occurrence of an Event of Default specified in Section 12.1(b), the Company and the Purchasers agree that a Holder will suffer damages and that it would not be feasible to ascertain the extent of such damages with precision. Accordingly, the Company agrees to pay liquidated damages ("Liquidated Damages") to each applicable Holder for any such continuing Event of Default, as follows: Liquidated Damages shall accrue on the principal amount of the Securities at a rate of $2.00 per calendar day per $1,000 principal amount of Debentures for the first 90 days immediately following each such Event of Default, and such Liquidated Damages shall increase by an additional $2.00 per calendar day per $1,000 principal amount of Debentures at the beginning of each subsequent 90-day period. As provided in Section 19.6 hereof, the remedy of Liquidated Damages shall be cumulative, and shall not exclude the availability of any other remedies hereunder or under the Transaction Documents (including, without limitation, the payment of late charges and default interest as provided in the Debentures).

12.3. 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 in favor of the Purchasers which is contained in any of the Transaction Documents 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 (including, without limitation, the right to enforce the Company Debenture Collateral, the Guaranties and the Guarantor Debenture Collateral, each in accordance with its respective terms). Each such holder agrees that it will give written notice to the other holders of Debentures 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 or in equity, by statute or otherwise.

ARTICLE XIII

INDEMNIFICATION

13.1. To the greatest extent permitted by applicable law, the Company agrees to indemnify each Purchaser against and hold it harmless from all claims, losses, damages, liabilities (or actions in respect thereof), obligations, penalties, awards, judgments, expenses (including, without limitation, reasonable fees and expenses of counsel) or disbursements (each a "Loss") arising out of or resulting from: (i) the breach of any representation or warranty of the Company in any Transaction Document or in any agreement, certificate or instrument delivered pursuant thereto; (ii) the breach of any agreement by the Company contained in any Transaction Document or any agreement, certificate of instrument delivered pursuant thereto; or (iii) Care Capital Investments II, LP 's and Essex Woodlands Health Ventures' representation on the Company's Board of Directors and any committees thereof or as an observer thereon.

13.2. Anything in Section 13.1 to the contrary notwithstanding, no claim may be asserted nor may any action be commenced against the Company for breach of any representation or warranty contained herein, unless notice of such Purchaser's intention to assert any such claim or commence any such action is received by the Company describing in writing in reasonable detail the facts and circumstances with respect to the subject matter of such claim or action on or prior to the date on which the representation or warranty on which such claim or action is based ceases to survive as set forth in Section 19.2. With respect to any claim or action as to which such notice shall have been given, the Purchasers shall be entitled to assert a claim or commence an action for indemnification with respect thereto at any time after the giving of such notice, regardless of whether any such claim or action may be asserted or commenced prior to or after the date on which the representation or warranty on which such claim or action is based ceases to survive as set forth in Section 19.2.

13.3. Such Purchaser agrees to give the Company prompt written notice of any claim, assertion, event or proceeding by a third party of which it has actual knowledge

concerning any Losses as to which it intends to request indemnification hereunder. The Company shall have the right to direct, through counsel of the Company's own choosing, the defense or settlement of any such claim or proceeding at the Company's own expense. If the Company elects to assume the defense of any such claim or proceeding, such Purchaser may participate in such defense, but in such case the expenses of such Purchaser shall be paid by such Purchaser. Such Purchaser shall cooperate with the Company in the defense or settlement thereof, and the Company shall reimburse such Purchaser for its reasonable out-of-pocket expenses in connection therewith. If the Company elects to direct the defense of any such claim or proceeding, such Purchaser shall not pay, or permit to be paid, any part of any claim or demand arising from such asserted liability, unless the Company consents in writing to such payment or unless the Company, subject to the last sentence of this Section 13.3, withdraws from the defense of such asserted liability, or unless a final judgment from which no appeal may be taken by or on behalf of the Company is entered against such Purchaser for such liability. If the Company shall fail to defend any such claim or proceeding, or if, after commencing or undertaking any defense, fails to prosecute or withdraws from such defense, such Purchaser shall have the right to undertake the defense or settlement thereof, at the Company's expense. If such Purchaser assumes the defense of any such claim or proceeding pursuant to this Section 13.3 and proposes to settle such claim or proceeding prior to a final judgment thereon or to forego appeal with respect thereto, then such Purchaser shall give the Company prompt written notice thereof and the Company shall have the right to participate in the settlement or assume or reassume the defense of such claim or proceeding.

ARTICLE XIV

AMENDMENT AND WAIVER

14.1. No amendment of any provision of this Agreement, including any amendment of this Article XIV, shall be valid unless the same shall be in writing and signed by (a) the Company, and each of Galen, Care Capital Investments II, LP or Essex Woodlands Health Ventures Fund V, so long as they (or their affiliates (as such term is defined in Rule 501(b)) shall hold Debentures, and (b) the holders of at least 51 % in the aggregate principal amount of the Debentures then outstanding, and no waiver by any party of any default, misrepresentation, or breach of warranty or covenant hereunder or under any other Transaction Document, whether intentional or not, shall be deemed to extend to any prior or subsequent default, misrepresentation, or breach of warranty or covenant hereunder or thereunder or affect in any way any rights arising by virtue of any prior or subsequent such occurrence.

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

ARTICLE XV

EXCHANGE OF DEBENTURES

15.1. Subject to Section 16.2, 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 19.5, 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.

15.2. Intentionally Omitted.

ARTICLE XVI

TRANSFER OF DEBENTURES

16.1. Notification of Proposed Sale. (a) Subject to Section 16.1(b), each holder of a Debenture by acceptance thereof agrees that it will give the Company ten 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 16.1(a).

16.2. Intentionally Omitted.

ARTICLE XVII

RIGHT OF FIRST REFUSAL; ADDITIONAL INVESTMENT

17.1. Right of First Refusal. Each holder of the Debentures, holder of Shares (provided any Debentures remain outstanding and the Shares received upon conversion have not been sold, transferred or otherwise disposed of) (the "Common Holder"), holders of the March 1998 Debentures (the "Existing 1998 Debentureholders") and holders of shares of Common Stock issued upon the conversion of the March 1998 Debentures (provided any March 1998 Debentures remain outstanding and the shares of Common Stock received upon conversion have

not been sold, transferred or otherwise disposed of) (the "Old Common Holders") shall be entitled to the following right of first refusal:

(a) Except in the case of Excluded Securities, the Company shall not issue, sell or exchange, agree to issue, sell or exchange, or reserve or set aside for issuance (except as provided in Section 6.16), sale or exchange (i) any shares of Common Stock, (ii) any other equity security of the Company, (iii) any debt security of the Company which by its terms is convertible into or exchangeable for, with or without consideration, any equity security of the Company, (iv) any security of the Company that is a combination of debt and equity or (v) any option, warrant or other right to subscribe for, purchase or otherwise acquire any equity security or any such debt security of the Company (collectively, the "Equity Securities") unless in each case, the Company shall have first offered to sell to the holders of Debentures, the Common Holders, the Existing 1998 Debentureholders and the Old Common Holders, the Equity Securities, at a price and on such other terms as shall have been specified by the Company in writing delivered to each of the holders of Debentures, the Common Holders, the Existing 1998 Debentureholders and the Old Common Holders (the "Offer"), which Offer by its terms shall remain open and irrevocable for a period of 30 days from the date it is delivered by the Company to the holders of Debentures, the Common Holders, the Existing 1998 Debentureholders and the Old Common Holders; provided, however, that such issuance, sale or exchange of equity securities shall result in gross proceeds to the Company (whether at the time of issuance or upon conversion, exercise, or exchange thereof) of an amount in excess of $200,000 (the "Minimum Offering Threshold"). For purposes of computing the Minimum Offering Threshold, all offerings, issuances, sales and exchanges of Equity Securities during any rolling 12-month period shall be aggregated.

(b) Each of the holders of Debentures, the Common Holders, the Existing 1998 Debentureholders and the Old Common Holders shall have the right to purchase up to its pro rata share of the Equity Securities determined at the time of the consummation of the Company's issuance of Equity Securities. The "pro rata share" of each holder of Debentures, Common Holder, Existing 1998 Debentureholders and the Old Common Holders shall be that amount of the Equity Securities multiplied by a fraction, the numerator of which is the sum of (i) Shares underlying the Debenture held by such Person if such Person is the holder of a Debenture, (ii) the number of Shares of Common Stock issued to such Common Holder upon conversion of a Debenture if such Person is a Common Holder, (iii) the number of shares of Common Stock underlying the March 1998 Debentures held by such Person if such Person is an Existing 1998 Debentureholder and (iv) the number of shares of Common Stock issued to an Existing 1998 Debentureholder upon conversion of a March 1998 Debenture if such Person is an Old Common Holder, and the denominator of which is the sum of (x) the total number of shares of Common Stock underlying the Debentures issued pursuant to this Agreement and (y) the total number of shares of Common Stock underlying the March 1998 Debentures.

(c) Notice of the intention of each holder of a Debenture, Common Holder, Existing 1998 Debentureholder or Old Common Holder to accept, in whole or in part, an Offer shall be evidenced by a writing signed by such person, as the case may be and delivered to the Company prior to the end of the 30-day period commencing with the date

of such Offer (or, if later within ten days after the delivery or giving of any written notice of a material change in such Offer), setting forth such portion (specifying number of shares, principal amount or the like) of the Equity Securities such Person elects to purchase (the "Notice of Acceptance").

(d) In the event that all holders of Debentures, Common Holders, Existing 1998 Debentureholders and Old Common Holders do not elect to purchase all of the Equity Securities, the persons which have provided notice of their intention to exercise the refusal rights as provided in subparagraph (c) above shall have the right to purchase, on a pro rata basis, any unsubscribed portion of the Equity Securities during a period of ten days following the 30-day period provided in subparagraph (c) above. Following such additional ten-day period, in the event the holders of the Debentures, the Common Holders, Existing 1998 Debentureholders and the Old Common Holders have not elected to purchase all of the Equity Securities, the Company shall have 90 days from the expiration of the foregoing 40-day period to sell all or any part of such Equity Securities as to which a Notice of Acceptance has not been given by any of such persons (the "Refused Securities") to any other Person or Persons on the terms provided in the Offer. Upon the closing of the sale to such other Person or Persons of all the Refused Securities, which shall include payment of the purchase price to the Company in accordance with the terms of the Offer, if the holders of Debentures, the Common Holders, Existing 1998 Debentureholders and Old Common Holders have timely submitted a Notice of Acceptance, it and they shall purchase from the Company, and the Company shall sell to such persons, as the case may be, the Equity Securities in respect of which a Notice of Acceptance was delivered to the Company, at the terms specified it the Offer. The purchase by the holders of Debentures, Common Holders, Existing 1998 Debentureholders and the Old Common Holders of any Equity Securities is subject in all cases to the preparation, execution and delivery by the Company to such persons of a purchase agreement and other customary documentation relating to such Equity Securities as is satisfactory in form and substance to such persons and each of their respective counsel.

(e) In each case, any Equity Securities not purchased by the holders of Debentures, the Common Holders, Existing 1998 Debentureholders and the Old Common Holders or by a Person or Persons in accordance with Section 17.1(d) hereof may not be sold or otherwise disposed of until they are again offered to such persons under the procedures specified in Sections 17.1(a), (c) and (d) hereof.

(f) The rights of the holders of Debentures, the Common Holders, Existing 1998 Debentureholders and the Old Common Holders under this Section 17.1 shall not apply to the following securities (the "Excluded Securities"):

(i) Common Stock or options to purchase such Common Stock, issued to officers, employees or directors of, or consultants to, the Company, pursuant to any agreement, plan or arrangement approved by the Board of Directors of the Company;

(ii) Common Stock issued as a stock dividend or upon any stock split or other subdivision or combination of shares of Common Stock;

(iii) shares issued upon conversion of the Debentures or the Existing Debentures or exercise of the warrants issued in connection with the issuance of the Existing Debentures;

(iv) any securities issued for consideration other than cash pursuant to a merger, consolidation, acquisition, strategic alliance or similar business combination approved by the Board of Directors and at the Company's Annual Meeting of Shareholders; or

(v) any debentures issued in satisfaction of interest payments under the Existing Debentures, including debentures instruments issued in satisfaction of interest payments on those debenture instruments.

(g) Notwithstanding anything to the contrary contained herein, a holder of a Debenture or a Common Holder (other than an initial Purchaser) shall not be considered as such for purposes of this Section 17.1 only, unless such Person then holds Debentures with an outstanding principal amount of at least $200,000 or Shares issued upon conversion of at least $200,000 in principal of Debentures or a combination of Debentures and Shares such that the outstanding principal of the Debentures held by such Person plus the amount of principal of Debentures converted into Shares held by such Person equals or exceeds $200,000.

ARTICLE XVIII

CO-SALE RIGHTS

18.1. In the event that Galen Partners, L.P., Galen Partners International III, L.P., Galen Employee Fund III, L.P., Oracle Strategic Partners L.P., Michael Reicher, Chief Executive Officer of the Company or Peter Clemens, Chief Financial Officer of the Company intends to transfer, directly or indirectly, in one or in a series of related transactions, any shares of the Company's Common Stock owned by it/him or any principal amount of the Existing Debentures or Debentures owned by it/him, such transferor (the "Selling Security Holder") shall notify the Holders in writing of such proposed transfer and its terms and conditions and within 15 business days of the date of such notice, each Holder shall notify the Selling Security Holder if such Holder elects to participate in the proposed transfer described in the written notice provided by the Selling Security Holder (a "Transfer"). Any Purchaser that fails to notify the Selling Security Holder within such 15 business day period shall be deemed to have waived its rights hereunder with respect to the Transfer described in the Selling Security Holder's written notice. Each Holder that notifies the Selling Security Holder that it intends to participate in the proposed Transfer, shall have the right to sell at the same price and on the same terms and conditions as the Selling Security Holder (a) in the case of a sale of shares of the Company's Common Stock by the Selling Security Holder, a number of shares of Common Stock equal to the shares of Common Stock proposed to be sold in the Transfer multiplied by a fraction, the numerator of which shall be the number of shares of Common Stock owned by the Holder (inclusive of all shares underlying the Debentures) and the denominator of which shall be the sum of (i) the Company's outstanding shares of Common Stock, plus (ii) the shares underlying the Debentures and the Existing Debentures, and (b) in the case of the proposed sale of Existing Debentures or Debentures by such Selling Security Holder, the principal amount of the Existing

Debentures or Debentures proposed to be sold in the Transfer multiplied by a fraction, the numerator of which shall be the aggregate principal amount of the Debentures owned by the Holder and the denominator of which shall be the aggregate principal amount of the Company's outstanding Existing Debentures and Debentures. Nothing in this Article XVIII shall be construed to limit the ability of the Selling Security Holder to complete the Transfer prior to the passage of ten business days notice period provided above, provided that sufficient accommodation is made to permit the Holders to complete the sale of their Common Stock and Debentures hereunder within ten business days of the election by such Holders to exercise their co-sale rights hereunder. The exercise or non-exercise of the rights of any Holder with respect to any particular Transfer shall not waive any such Holder's rights to participate in a subsequent Transfer.

ARTICLE XIX

MISCELLANEOUS

19.1. 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, excluding to the greatest extent permitted by law any rule of law that would cause the application of the laws of any jurisdiction other than the State of New York.

19.2. Survival of Representations. Subject to the terms of this Agreement, the representations, warranties, covenants and agreements contained, in the Transaction Documents and in any agreements, certificates or other instruments delivered pursuant thereto shall survive (a) any investigation made by or on behalf the Purchasers and (b) the Closing until the maturity date of the Debentures (as such date may be extended by the parties).

19.3. 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 parties hereto and their respective successors, assigns, heirs, executors and administrators. No party may assign any of its rights hereunder without the prior written consent of the other parties; provided, however, that any Purchaser may assign any of its rights under any of the Transaction Documents to (a) any "affiliate" (as such term is defined in Rule 501(b)) of such Purchaser or (b) any Person to whom such Purchaser shall transfer any Securities in accordance with the terms of the Transaction Documents; provided further, that notwithstanding anything herein or in the Transaction Documents to the contrary, no opinion of counsel shall be necessary for a transfer or assignment of the Debentures or any rights under any of the Transaction Documents (except for the Watson Warrant) by a Purchaser that is a partnership, corporation or limited liability company to any general partner, limited partner, retired partner, shareholder, member, retired member, officer, director or affiliates of such Purchaser, or the members or retired members of the foregoing, as applicable, or the estates, beneficiaries and family members of any such general partner, limited partners, retired partners, shareholders, members, retired members, officers, directors and affiliates and any trusts for the benefit of any of the foregoing persons, provided, that in each case the transferee will be subject to the applicable terms of the Transaction Documents to the same extent as such transferee were an original Purchaser hereunder.

19.4. Entire Agreement. This Agreement (including the Exhibits and Schedules hereto), the other Transaction Documents and any 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.

19.5. 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 61107
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 Wolf, Block, Schorr and Solis-Cohen LLP, 250 Park Avenue, New York, New York 10177 Attn.: George N. Abrahams, Esq., Facsimile: (212) 672-1109, or such other address as may be directed.

19.6. Delays, Omissions or Waivers. 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. Notwithstanding anything set forth herein or in any Transaction Document, if the consent of or the waiver by any 2002 Holder is needed or otherwise desirable under any

Transaction Document and the Company, or any affiliate thereof, pays or other gives consideration to any 2002 Holder, or an affiliate thereof, for such consent or waiver the Company shall offer the same to all other 2002 Holders.

19.7. Independence of Covenants and Representations and Warranties. All covenants hereunder shall be given independent effect so that if a certain action or condition constitutes a default under a certain covenant, the fact that such action or condition is permitted by another covenant shall not affect the occurrence of such default. In addition, all representations and warranties hereunder shall be given independent effect so that if a particular representation or warranty proves to be incorrect or is breached, the fact that another representation or warranty concerning the same or similar subject matter is correct or is not breached will not affect the incorrectness of or a breach of a representation and warranty hereunder.

19.8. 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.

19.9. Agent's Fees. (a) Except as provided in Section 19.9 of the Schedule of Exceptions, 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, 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 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 (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.

19.10. 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. Such reimbursement shall be paid on the Closing Date.

19.11. Jurisdiction. (a) Each of the parties hereto hereby irrevocably and unconditionally submits, for itself and its property, to the nonexclusive jurisdiction of any New York State court or United States Federal court sitting in New York City, and any appellate court from any thereof, in any action or proceeding arising out of or relating to this Agreement or any of the other Transaction Documents to which it is a party or to whose benefit it is entitled, or for recognition or enforcement of any judgment, and each of the parties hereto irrevocably and unconditionally agrees that all claims in respect of any such action or proceeding may be heard and determined in any such New York State court or, to the fullest extent permitted by law, in such United States Federal court. Each of the parties hereto agrees that a final judgment in any such action or proceeding shall be conclusive and may be enforced in other jurisdictions by suit on the right that any party may otherwise have to bring any action or proceeding relating to this Agreement or any of the other Transaction Documents in the courts of any other jurisdiction.

(b) Each of the parties hereto irrevocably and unconditionally waives, to the fullest extent it may legally and effectively do so, any objection that it may now or hereafter have to the laying of venue of any suit, action or proceeding arising out of or in relation to this Agreement or any other Transaction Document to which it is a party in any such New York State or United States Federal court sitting in New York City. Each of the parties hereto hereby irrevocably waives, to the fullest extent permitted by law, the defense of an inconvenient forum to the maintenance of such action or proceeding in any such court.

19.12. Waiver of Jury Trial. EACH OF THE PARTIES HERETO HEREBY IRREVOCABLY WAIVES ALL RIGHT TO TRIAL BY JURY IN ANY ACTION, PROCEEDING OR COUNTERCLAIM (WHETHER BASED ON CONTRACT, TORT OR OTHERWISE) ARISING OUT OF OR RELATING TO ANY TRANSACTION DOCUMENT OR THE ACTIONS OF ANY PARTY IN THE NEGOTIATION, ADMINISTRATION, PERFORMANCE OR ENFORCEMENT THEREOF.

19.13. Confidentiality. (a) Each of the Purchasers hereby agrees to keep (and to cause its affiliates, employees, agents, attorneys, accountants and other professional advisors to keep) confidential the confidential information provided to it by or on behalf of the Company or its Subsidiaries pursuant to or in connection with the Agreement or any other Transaction Document, provided that, such information may be disclosed (i) solely in connection with the performance of the transactions contemplated by this Agreement and any other Transaction Document to (A) its affiliates, directors, officers and employees who have a need to know such information and its agents, attorneys, accountants and other professional advisors or (B) the other Purchasers, (ii) in response to any order of any court or other governmental or administrative body or agency or as may be required by any law binding upon any of the Purchasers, (iii) in connection with the exercise of any remedies under any Transaction Document or the enforcement of rights hereunder and thereunder, (iv) with the consent of the Company or (v) to

the extent such information (A) is on the date hereof, or at or before the time such disclosure becomes, publicly available other than as a result of a breach by such disclosing Person of the obligation set forth in this Agreement or (B) at or before the time of such disclosure becomes available to any Purchaser on a nonconfidential basis from a source other than the Company or its Subsidiaries, which source is not known to the recipient of such information to have breached a confidentiality agreement with the Company or its Subsidiaries in respect of such information.

(b) Each Purchaser hereby agrees that in the event such Purchaser is requested or required other than by applicable law (by interrogatory, request for information or documents, subpoena, deposition, civil investigative demand or other process) to disclose any information pursuant to clause (ii) above, such Purchaser will, except to the extent such notice would cause such Purchaser to be in violation of law, provide the Company with prompt notice of any such request or requirement so that the Company may seek an appropriate protective order or other similar assurance to prevent disclosure of such information or waive compliance with the provisions of this Section 19.13. Such Purchaser may not oppose action by the Company to obtain an appropriate protective order or other reliable assurance that confidential treatment will be accorded such information, provided that such Purchaser may oppose the Company's action to obtain an appropriate protective order or other reliable assurance in the event that, in connection with any action, suit or other legal or equitable proceeding (including any bankruptcy proceeding), such Purchaser reasonably believes that the failure to publicly disclose such information would materially and adversely affect such Purchaser's ability to protect or exercise its rights and remedies hereunder or under any other Transaction Document.

(c) The Purchasers may also disclose, subject to their compliance with the requirements of clause (b) above, such information to the extent the Purchasers reasonably believe it is appropriate to in connection with any action, suit or other legal or equitable proceeding (including any bankruptcy proceeding) to protect or otherwise exercise their rights and remedies hereunder or under any other Transaction Document in any legal or equitable proceeding.

(d) In furtherance to the foregoing, each of the Purchasers agrees that its right to request any information pursuant to Section 9.2(g) or to avail itself of the provisions of Section 9.6(b) shall be conditioned on its continuing compliance with the requirements of this Section 19.13.

19.14 Prohibition on Certain Cash Interest Payments. Each of the Company, Galen and Oracle Strategic Partners, L.P., agree that the Company shall not make any cash interest payments to Galen or Oracle Strategic Partners, L.P., pursuant to the March 1998 Debentures or the May 1999 Debentures, notwithstanding anything else to the contrary contained therein or elsewhere, without the prior written consent of all 2002 Holders, which consent shall be within their sole and absolute discretion.

19.15 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.

19.16 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.

ARTICLE XX

CERTAIN DEFINED TERMS

As used in this Agreement, the following terms shall have the following meanings:

"Agreement" means this Debenture Purchase Agreement, dated as of December 20, 2002, between the Company, Care Capital Investments II, LP, Essex Woodlands Health Ventures and the other Purchasers listed on the signature page hereto.

"Alternative Arrangement" has the meaning specified in Section 12.1(i) of this Agreement.

"AMEX" has the meaning specified in Section 9.2(g) of this Agreement.

"Approved Accounting Firm" has the meaning specified in Section 9.6(d) of this Agreement.

"ARCOS" means the Automation of Reports and Consolidated Orders System which monitors the flow of DEA controlled substances from their point of manufacture to point of sale or distribution.

"Arm's Length" has the meaning specified in Section 10.5 of this Agreement.

"Change of Control" means the occurrence of any of the following: (a) the consummation of any transaction the result of which is that any Person or group (as such term is used in Section 13(d)(3) of the Exchange Act), other than Galen or any affiliate thereof or any group comprised of any of the foregoing, owns, directly or indirectly, 51% of the Common Equity of the Company, (b) the Company consolidates with, or merges with or into, another Person (other than a direct or indirect wholly owned Subsidiary) or sells, assigns, conveys, transfers, leases or otherwise disposes of all or substantially all of the Company's assets or the assets of the Company and its Subsidiaries taken as a whole to any person, or any Person consolidates with, or merges with or into, the Company, in any such event pursuant to a transaction in which the outstanding Voting Stock of the Company, as the case may be, is converted into or exchanged for cash, securities or other property, other than any such transaction where the outstanding Voting Stock of the Company, as the case may be, is converted into or exchanged for Voting Stock of the surviving or transferee corporation and the beneficial owners of the Voting Stock of the Company immediately prior to such transaction own, directly or indirectly, not less than a majority of the Voting Stock of the surviving or transferee corporation immediately after such transaction, (c) the Company, either individually or in conjunction with one or more Subsidiaries sells, assigns, conveys, transfers, leases or otherwise disposes of, or the Subsidiaries sell, assign, convey, transfer, lease or otherwise dispose of, all or

substantially all of the properties and assets of the Company and its Subsidiaries, taken as a whole (either in one transaction or a series of related transactions), including capital stock of the Subsidiaries, to any Person (other than the Company or a wholly owned Subsidiary of the Company), or (d) during any two year period commencing subsequent to the date of this Agreement, individuals who at the beginning of such period constituted the Board of Directors of the Company (together with any new directors whose election by such Board of Directors or whose nomination for election by the stockholders of the Company was approved by the directors then still in office) who were either directors at the beginning of such period or whose election or nomination for election was previously so approved cease for any reason to constitute a majority of the Board of Directors then in office; provided, however, that a Person shall not be deemed to have ceased being a director for such purpose if such Person shall have resigned or died or if the involuntary removal of such Person was made at the direction of persons holding a majority in principal amount of the outstanding Debentures. For purposes of this definition, (i) the term "Common Equity" of the Company means all capital stock of the Company that is generally entitled to vote in the election of members of the Board of Directors and (ii) the term "Voting Stock" of the Company means securities of any class of capital stock of the Company entitling the holders thereof to vote in the election of members of the Board of Directors.

"Closing" and "Closing Date" have the respective meanings specified in Article III of this Agreement.

"Code" has the meaning specified in Section 4.18(a) of this Agreement.

"Commission" has the meaning specified in Section 4.8(a) of this Agreement.

"Common Holder" has the meaning specified in Section 17.1 of this Agreement.

"Common Stock" has the meaning specified in Section 1.1 of this Agreement.

"Company" means Halsey Drug Co., Inc., a New York corporation.

"Company Debenture Collateral" has the meaning specified in Section 2.2.

"Company General Security Agreement" has the meaning specified in Section 2.2(a) of this Agreement.

"Company Reports" has the meaning specified in Section 4.10 of this Agreement.

"Core Products Agreement" has the meaning specified in Section 12.1(i) of this Agreement.

"CSA" has the meaning specified in Section 4.10(c) of this Agreement.

"D&O Insurance" has the meaning specified in Section 9.14 of this Agreement.

"DEA" has the meaning specified in Section 4.10(c) of this Agreement.

"Debenture Dilution Waiver" means the Debenture Dilution Waiver to be signed by each of the Existing Debentureholders prior to the Closing Date serving to waive the dilution adjustments provisions of the Existing Debentures and the common stock purchase warrants issued with the Existing Debentures relating to the issuance of the Common Stock by the Company in accordance with the Recapitalization Agreement.

"Debentures" has the meaning specified in Section 1.1 of this Agreement.

"Debentureholders Agreement" means the Debentureholders Agreement (as such agreement may be supplemented, amended or otherwise modified from time to time in accordance with its terms) dated as of December 20, 2002 between the Company, the holders of the Existing Debentures and the Purchasers substantially in the form attached as Exhibit K hereto.

"Default Notice" has the meaning specified in Section 12.1(c) of this Agreement.

"Designee" has the meaning specified in Section 9.7 of this Agreement.

"ERISA" has the meaning specified in Section 4.18(a) of this Agreement.

"ERISA Affiliates" has the meaning specified in Section 4.18(a) of this Agreement.

"Exchange Act" has the meaning specified in Section 4.8(a) of this Agreement.

"Excluded Securities" has the meaning specified in Section 17.1(f) of this Agreement.

"Existing 1998 Debentureholders" has the meaning specified in Section 17.1 of this Agreement.

"Existing Debentures" means, collectively, the March 1998 Debentures and the May 1999 Debentures, as such debentures may be supplemented, amended or otherwise modified from time to time, including, without limitation, by the Existing Debenture Amendments.

"Existing Debenture Amendments" has the meaning specified in Section 6.7 of this Agreement.

"Existing Debentureholders Consent" has the meaning specified in Section 6.7 of this Agreement.

"Event of Default" has the meaning specified in Section 12.1 of this Agreement.

"FDA" has the meaning specified in Section 4.10(b) of this Agreement.

"FDC Act" has the meaning specified in Section 4.10(b) of this Agreement.

"412 Plan" has the meaning specified in Section 4.18(d) of this Agreement.

"Galen" has the meaning specified in Section 2.2(a) of this Agreement.

"Galen Bridge Lenders" means, collectively, Galen and the other lenders pursuant to that certain Galen Bridge Loan Agreement.

"Galen Bridge Lenders' Consent" has the meaning specified in Section 6.8 of this Agreement.

"Galen Bridge Loan Agreement" means the Bridge Loan Agreement dated as of August 15, 2001 (as amended on January 9, 2002, April 15, 2002 and May 8, 2002, and as further supplemented, amended or otherwise modified from time to time in accordance with its terms) between the Company, Galen and certain other lenders listed on the signature pages thereto.

"Galen Bridge Notes" means the 10% convertible senior secured promissory notes issued by the Company to the Galen Bridge Lenders under the Galen Bridge Loan Agreement.

"Guaranty" and "Guaranties" has the meaning specified in Section 2.3 of this Agreement.

"Guarantor" has the meaning specified in Section 2.3 of this Agreement.

"Guarantor Debenture Collateral" has the meaning specified in Section 2.4 of this Agreement.

"Guarantors Security Agreement" has the meaning specified in Section 2.4(a) of this Agreement.

"Holders" shall mean the Purchasers or any Person to whom a Purchaser or transferee of a Purchaser has assigned, transferred or otherwise conveyed any Debenture or Shares.

"Immaterial Subsidiaries" means Blue Cross Products, Inc., The Medi-Gum Corporation, H.R. Cenci Laboratories, Inc., and Cenci Powder Products, Inc.

"Indebtedness" has the meaning specified in Section 10.4 of this Agreement.

"Insurance Organizations" has the meaning specified in Section 4.20 of this Agreement.

"Institutional Existing Debentureholders" has the meaning provided in Section 6.16 of this Agreement.

"Institutional Existing Debentureholders Reserved Shares" has the meaning provided in Section 6.16 of this Agreement.

"Intellectual Property Rights" has the meaning specified in Section 4.12(a) of this Agreement.

"Joinder Agreement" was the meaning specified in Article III of this Agreement.

"IRS" has the meaning specified in Section 4.18(b) of this Agreement.

"Leased Property" has the meaning specified in Section 4.20 of this Agreement.

"Leases" has the meaning specified in Section 4.20 of this Agreement.

"Loss" has the meaning specified in Section 13.1 of this Agreement.

"March 1998 Debentures" means the 5% convertible secured debentures due March 15, 2003 (as such debentures may be supplemented, amended, or otherwise modified from time to time) issued pursuant to that certain Debenture and Warrant Purchase Agreement dated March 10, 1998 between the Company and the Purchasers listed on the signature page thereto.

"Material Adverse Effect" has the meaning specified in Section 4.1 of this Agreement.

"May 1999 Debentures" means the 5% convertible secured debentures due March 15, 2003 (as such debentures may be supplemented, amended, or otherwise modified from time to time) issued pursuant to that certain Debenture and Warrant Purchase Agreement dated May 26, 1999 between the Company and the Purchasers listed on the signature page thereto.

"Minimum Offering Threshold" has the meaning specified in Section 17.1(a) of this Agreement.

"Mortgage" has the meaning specified in Section 2.4(c) of this Agreement.

"Mortgage Subordination Agreement" shall mean that certain Subordination Agreement, dated the date hereof, between Houba, Galen and Oracle Strategic Partners, L.P. relating to real property owned by Houba.

"NASDAQ" has the meaning specified in Section 9.2(g) of this Agreement.

"Offer" has the meaning specified in Section 17.1(a) of this Agreement.

"Old Common Holders" has the meaning specified in Section 17.1 of this Agreement.

"Owned Property" has the meaning specified in Section 4.20 of this Agreement.

"PBGC" has the meaning specified in Section 4.18(b) of this Agreement

"PCB" has the meaning specified in Section 4.16(c) of this Agreement.

"Permitted Liens" has the meaning specified in Section 10.3(l) of this Agreement.

"Person" means any individual, corporation, limited liability company, partnership, association, trust or any other entity or organization, including a government or political subdivision or an agency or instrumentality thereof.

"Plan" has the meaning specified in Section 4.18(a) of this Agreement.

"Purchaser" has the meaning specified in Section 1.1 of this Agreement.

"Real Property Permits" has the meaning specified in Section 4.20 of this Agreement.

"Recapitalization Agreement" has the meaning specified in Section 6.9 of this Agreement.

"Refused Securities" has the meaning specified in Section 17.1(d) of this Agreement.

"Registration Rights Agreement" means that certain Registration Rights Agreement, dated the date hereof, between the Company, the Purchasers, Watson, the holders of the March 1998 Debentures, the holders of the May 1999 Debentures and the other parties listed on Schedule 1 thereto.

"Remaining Galen Warrants" has the meaning provided in Section 1.2.

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.

"Rule 501(b)" has the meaning specified in Article III of this Agreement.

"Schedule of Exceptions" has the meaning specified in Article IV of this Agreement.

"Securities" has the meaning specified in Section 1.1 of this Agreement.

"Securities Act" has the meaning specified in Section 4.8(a) of this Agreement.

"Security Interest Termination Date" shall mean the first date on which each of the following events shall have occurred: (a) all of the Company's and the Guarantors' obligations and liabilities under the Transaction Documents (except for the Watson Term Loan Amendment, the 2002 Watson Term Loan, the Registration Rights Agreement, the Watson Consent, the Watson Supply Agreement, the Watson Supply Agreement Amendment, the Watson Warrant, the Existing Debenture Amendments and the Existing Debentureholder Consent) shall have been either or both of (i) indefeasibly paid in full or, as applicable, indefeasibly discharged, or (ii) irrevocably converted in accordance with this Agreement and the Debentures, (b) none of the Company's or Guarantors' obligations or liabilities (whether actual or contingent) shall remain outstanding, except (with respect to subsection (a) and this subsection (b)) for the Company's obligations

under the Registration Rights Agreement, and (c) Galen, acting as agent for the Purchasers under the applicable Transaction Documents, shall have delivered written notification to the Company and the Guarantors of the satisfaction of the conditions in subsections (a) and (b) above.

"Selling Security Holder" has the meaning specified in Section 18.1 of this Agreement.

"Shareholders Meeting Date" means that date on which the shareholders and the debentureholders amend the Company's Certificate of Incorporation to increase the number of authorized shares of the Common Stock available for issuance from 80,000,000 to such number of shares as shall equal the sum of (a) the Company's issued and outstanding Common Stock, plus (b) the number of shares of Common Stock issuable upon the conversion and exercise of the Company's outstanding convertible securities, plus (c) the number of shares of Common Stock issuable upon conversion of the Debentures and exercise of the Watson Warrant , plus (d) 50 million shares, as shall sum shall be rounded up to the nearest whole five million shares.

"Shares" has the meaning specified in Section 1.1 of this Agreement.

"Solvent" has the meaning specified in Section 4.22 of this Agreement.

"Stock Pledge Agreement" has the meaning specified in Section 2.2(a) of this Agreement.

"Subordination Agreement" has the meaning specified in Section 6.6 of this Agreement.

"Subsidiary" has the meaning specified in Section 4.2 of this Agreement.

"Termination Date" has the meaning specified in Section 1.2(b) of this Agreement.

"2000 Watson Term Loan" means that certain Term Loan Agreement for an aggregate principal amount of $17,500,000 between the Company and Watson dated March 29, 2000, as such agreement may be supplemented, amended or otherwise modified from time to time, including, without limitation, by the Watson Term Loan Amendment.

"2002 Holder" has the meaning set forth in Article III of this Agreement.

"2002 Watson Term Loan" has the meaning specified in Section 6.6 of this Agreement.

"Transaction Documents" has the meaning specified in Section 4.4(a) of this Agreement.

"Transfer" has the meaning specified in Section 18.1 of this Agreement.

"Unfunded Pension Liability" has the meaning specified in Section 4.18(e) of this Agreement.

"US GAAP" has the meaning specified in Section 4.8(a) of this Agreement.

"Voting Agreement" has the meaning specified in Section 9.12(b) of this Agreement.

"Watson" means Watson Pharmaceuticals, Inc., a Nevada corporation.

"Watson Consent" has the meaning specified in Section 6.6 of this Agreement.

"Watson Supply Agreement " means the Finished Goods Supply Agreement (Core Products) dated March 29, 2000, as amended by that certain Amendment and Supplement No. 1 to Finished Goods Supply Agreement (Core Products) dated August 8, 2001.

"Watson Supply Agreement Amendment" has the meaning specified in Section 6.6 of this Agreement.

"Watson Term Loans" mean that certain (a) 2000 Watson Term Loan and (b) 2002 Watson Term Loan for an aggregate principal amount of $3,901,331.

"Watson Term Loan Amendment" has the meaning specified in Section 6.6 of this Agreement.

"Watson Warrant" means a Common Stock Purchase Warrant issued by the Company to Watson on the Closing Date exercisable for 10,700,665 shares of Common Stock at an exercise price per share equal to the conversion price of the Debentures.

"Withdrawal Liability" has the meaning specified in Section 4.18(g) of this Agreement.

[SIGNATURE PAGES TO FOLLOW]

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:

Michael Reicher
Chief Executive Officer

Solely as to the Provisions of
Sections 9.12(b) and 19.14 and Articles XVIII and XIX hereof

GALEN PARTNERS III, L.P.
BY: CLAUDIUS, L.L.C., GENERAL PARTNER

By:

Srini Conjeevaram
General Partner

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

By:

Srini Conjeevaram
General Partner

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

By:

Bruce F. Wesson
General Partner

ORACLE STRATEGIC PARTNERS, L.P.

By:

Name:
Title:

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

- ---
By: Michael K. Reicher
Its: Trustee

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

- ---
By: Robert W. Baird
Its: Trustee

- ---
Peter Clemens

PURCHASERS

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

- ----------

By: Srini Conjeevaram
Its: General Partner

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

By: Srini Conjeevaram
Its: General Partner

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

- ----------

By: Bruce F. Wesson
Its: General Partner

ESSEX WOODLANDS HEALTH
VENTURES V, L.P.
By: Essex Woodlands Health Ventures V, L.L.C.,
its General Partner
190 South LaSalle Street, Suite 2800
Chicago, IL 60603

By: Immanuel Thangaraj
Its: Managing Director

CARE CAPITAL INVESTMENTS, L.P.
By: Care Capital, L.L.C., General Partner
Princeton Overlook One
100 Overlook Center, Suite 102
Princeton, New Jersey 08540

- ----------

By:
Its:

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

MICHAEL WEISBROT
1136 Rock Creek Road
Gladwyne, Pennsylvania 19035

- ----------

SUSAN WEISBROT
1136 Rock Creek Road
Gladwyne, Pennsylvania 19035

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

ROGER GRIGGS
c/o Tom Jennings
7300 Turfway Road
Suite 300
Florence, KY 41042

- ----------

GEORGE E. BOUDREAU
222 Elbow Lane
Haverford, PA 19041

- ----------

EXHIBIT A

LIST OF PURCHASERS AND

ALLOCATION OF SECURITIES

EXHIBIT B

FORM OF DEBENTURE

EXHIBIT C

SCHEDULE OF EXCEPTIONS

EXHIBIT D

SUBSCRIPTION AGREEMENT

EXHIBIT E

COMPANY GENERAL SECURITY AGREEMENT

EXHIBIT F

GUARANTY AGREEMENT

EXHIBIT G

GUARANTORS SECURITY AGREEMENT

EXHIBIT H

LEGAL OPINION

EXHIBIT I

VOTING AGREEMENT

EXHIBIT J

FORM OF JOINDER AGREEMENT

EXHIBIT K

DEBENTUREHOLDERS AGREEMENT

EXHIBIT L

STOCK PLEDGE AGREEMENT

EXHIBIT M

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EXHIBIT N

RECAPITALIZATION AGREEMENT

EXHIBIT O

REMAINING GALEN ENTITIES WARRANTS

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HALSEY DRUG CO., INC.

$ 35,000,000

5% CONVERTIBLE SENIOR SECURED DEBENTURE

DUE MARCH 31, 2006

HALSEY DRUG CO., INC.

DEBENTURE PURCHASE AGREEMENT

DATED AS OF DECEMBER 20, 2002

EXHIBIT 10.2

HALSEY DRUG CO., INC.

COMPANY GENERAL SECURITY AGREEMENT

THIS COMPANY GENERAL SECURITY AGREEMENT ("Company Security Agreement") is made and entered into as of December 20, 2002 by and between HALSEY DRUG CO., INC., a New York corporation (the "Debtor"), with its principal place of business at 695 North Perryville Road, Rockford, Illinois 61107, and GALEN PARTNERS III, L.P., a Delaware limited partnership ("Galen"), with its principal place of business at 610 Fifth Avenue, 5th Floor, New York, New York 10020 acting in its capacity as agent for the Purchasers (as such term is defined below) (in such capacity, the "Agent") for the benefit of the Purchasers.

W I T N E S S E T H

WHEREAS, Galen, certain other purchasers (together with Galen, the "Purchasers") and the Debtor have entered into a Debenture Purchase Agreement dated as of the date hereof (as the same may be amended, modified, supplemented or restated from time to time, the "Purchase Agreement"; terms which are capitalized herein and not otherwise defined shall have the meanings ascribed to them in the Purchase Agreement); and

WHEREAS, the Purchasers have required, as a condition precedent to the effectiveness of the Purchase Agreement, that the Debtor (i) grant to the Agent, for the ratable benefit of the Purchasers, a security interest in and to the Collateral (as defined in Section II below) and (ii) execute and deliver this Company Security Agreement in order to secure the payment and performance by the Debtor of the obligations owing by the Debtor to the Purchasers under the Purchase Agreement, the Debentures, the other Transaction Documents (as defined in the Subordination Agreement) and each of the agreements, documents and instruments delivered by the Debtor pursuant thereto or in connection therewith (collectively, the "Obligations").

NOW, THEREFORE, in consideration of the premises and in order to induce the Purchasers to enter into and perform the Purchase Agreement, the Debtor hereby agrees as follows:

SECTION I. CREATION OF SECURITY INTEREST.

A. Security Interest. The Debtor hereby pledges, assigns and grants to the Agent a continuing perfected lien and security interest, having priority over any and all other security interests (except as otherwise provided in the Subordination Agreement), in all of the Debtor's right, title and interest in and to the Collateral in order to secure the payment and performance of all Obligations owing by the Debtor.

B. Debtor Remains Liable. Anything herein to the contrary notwithstanding, (i) the Debtor shall remain liable under the contracts and agreements included in the Debtor's Collateral to the extent set forth therein to perform all of its duties and obligations thereunder to the same extent as if this Company Security Agreement had not been executed, (ii) the exercise by the Agent

of any of the rights hereunder shall not release the Debtor from any of its duties or obligations under the contracts and agreements included in the Collateral and (iii) neither the Agent nor any Purchaser shall have any obligation or liability under the contracts and agreements included in the Collateral by reason of this Company Security Agreement, the Purchase Agreement or any other Transaction Document, nor shall the Agent or any Purchaser be obligated to perform any of the obligations or duties of the Debtor thereunder or to take any action to collect or enforce any claim for payment assigned hereunder.

SECTION II. COLLATERAL.

For purposes of this Company Security Agreement, the term "Collateral" shall mean all of the kinds and types of property described in subsections A. through G. of this Section II, whether now owned or hereafter at any time arising, acquired or created by the Debtor and wherever located, and includes all replacements, additions, accessions, substitutions, repairs, proceeds and products relating thereto or therefrom, and all documents, ledger sheets and files of the Debtor relating thereto and all Proceeds of Collateral. "Proceeds" hereunder include (i) whatever is now or hereafter received by the Debtor upon the sale, exchange, collection or other disposition of any item of Collateral, whether such proceeds constitute inventory, accounts, accounts receivable, general intangibles, instruments, securities (including, without limitation, United States of America Treasury Bills), credits, claims, demands, documents, letters of credit and letter of credit proceeds, chattel paper, documents of title, certificates of title, certificates of deposit, warehouse receipts, bills of lading, leases, deposit accounts, money, tax refund claims, contract rights, royalties, goods, equipment, payment under insurance (whether or not the Agent is the loss payee thereof), or any indemnities, warranties or guaranties, payable by reason of loss or damage to or otherwise with respect to any or the foregoing Collateral, and (ii) any such items which are now or hereafter acquired by the Debtor with any proceeds of Collateral hereunder.

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

B. Inventory. All of the Debtor's inventory, including without limitation (i) all raw materials, work in process, parts, components, assemblies, supplies and materials used or consumed in the Debtor's businesses, wherever located and whether in the possession of the Debtor or any other Person (for the purposes of this Company Security Agreement, the term "Person" "Person" means any individual, sole proprietorship, partnership, joint venture, trust, unincorporated organization, association, corporation, limited liability company, institution, entity, party or government, including any division, agency or department thereof); (ii) all goods, wares and merchandise,

finished or unfinished, held for sale or lease or leased or furnished or to be furnished under contracts of service, wherever located and whether in the possession of the Debtor or any other Person or entity; and (iii) all goods returned to or repossessed by the Debtor (all of the foregoing property being hereinafter referred to as "Inventory");

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

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

E. Intellectual Property. All of the Debtor's intellectual property, including, without limitation, New Drug Applications, Investigatory New Drug Applications, Abbreviated New Drug Applications, Alternative New Drug Applications, registrations and quotas as issued by the Drug Enforcement Administration and/or the Attorney General of the United States pursuant to the Controlled Substances Act, certifications, permits and approvals of federal and state governmental agencies, patents, patent applications, trademarks, trademark applications, service marks, service mark applications, trade names, domain names, technical knowledge and processes, formal or informal licensing arrangements which are permitted to be assigned or pledged, blueprints, technical specifications, computer software, programs, databases, copyrights, copyright applications and all confidential and proprietary information, including, without limitation, know-how, trade secrets, manufacturing and production processes and techniques, inventions, research and development information, databases and data, including, without limitation, technical data, financial and marketing and business data, pricing and cost information and business and marketing plans, and all embodiments thereof, and rights thereto, including, without limitation, all of the Debtor' rights to use the patents, trademarks, copyrights, service marks, or other property of the aforesaid nature of other Persons now or hereafter licensed to the Debtor, together with the goodwill of the business symbolized by or connected with the Debtor's trademarks, copyrights, service marks, licenses and the other rights included in this Section II(E).

F. Distributions. All interest, dividends, distributions, cash, instruments and other property from time to time received, receivable or otherwise distributed in respect of or in exchange for any or all of the then existing Collateral.

G. Subsidiaries. All of the shares of stock or other securities of Houba, Inc. and Halsey Pharmaceuticals, Inc., and the certificates, if any, representing such shares or other securities, and all dividends, distributions, return of capital, cash, instruments and other property from time to time received, receivable or otherwise distributed in respect of or in exchange for any or all of such shares or securities and all subscription warrants, rights or options issued thereon or with respect

thereto, and all Investment Property, all, to the extent applicable, as further set forth in the Stock Pledge Agreement.

SECTION III. THE DEBTOR'S REPRESENTATIONS AND WARRANTIES.

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

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

C. Restrictions on Collateral Disposition. None of the Collateral is subject to contractual obligations that may restrict or inhibit the Agent's rights or ability to sell or dispose of the Collateral or any part thereof after the occurrence of an Event of Default except (i) the rights of Watson under the Watson Loan Agreement and the documents executed in connection therewith, including, without limitation, the Watson Security Agreement dated as of March 29, 2000 (the "Watson Security Agreement"); (ii) the rights of the investors in the 5% convertible senior secured debentures due March 31, 2006 issued pursuant to a certain Debenture and Warrant Purchase Agreement dated March 10, 1998, as amended, between the Company and the purchasers listed on the signature page thereto (the "March 1998 Debentures"); and (iii) the rights of the investors in the 5% convertible senior secured debentures due March 31, 2006 issued pursuant to a curtain Debenture and Warrant Purchase Agreement dated May 26, 1999, as amended, between the Company and the purchasers listed on the signature page thereto (the "May 1999 Debentures").

D. Status of Accounts. Each Account is based on an actual and bona fide rendition of services or sale of goods/products to customers, made by the Debtor in the ordinary course of its business; the Accounts created are its exclusive property and are not and shall not be subject to any lien, consignment arrangement, encumbrance, security interest or financing statement whatsoever, except (i) the lien in favor of Watson under the Watson Loan Agreement and the documents executed in connection therewith, including, without limitation, the Watson Security Agreement, (ii) the lien in favor of the investors in the March 1998 Debentures and (iii) the lien in favor of the investors in the May 1999 Debentures, and to the best knowledge of the Debtor, the Debtor's customers have accepted the goods/products and services, and owe and are obligated to pay the full amounts stated in the invoices according to their terms, without any dispute, offset, defense or counterclaim.

E. Copyrights, Trademarks and Patents.

(i) Debtor owns outright all of the Intellectual Property Rights listed on Section 4.12 of the Schedule of Exceptions attached to the Purchase Agreement 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.

(ii) Debtor has not licensed to anyone the use of 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 of third parties.

(iii) The Debtor has no knowledge, nor has it received any notice (a) 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 (b) that the Intellectual Property Rights infringe upon the rights of any third party.

(iv) The Debtor has made or performed all filings, recordings and other acts and has paid all required fees and taxes to maintain and protect its interest in each and every item of intellectual property in full force and effect throughout the world, and to protect and maintain its interest therein including, without limitation, recordations of any of its interests in patents and trademarks with the U.S. Patent and Trademark Office and in corresponding national and international patent offices, and recordation of any of its interests in any copyrights with the U.S. Copyright Office and in corresponding national and international copyright offices. The Debtor has used proper statutory notice in connection with its use of each patent, trademark and copyright.

F. Inventory. All inventory of the Debtor 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 Debtor and its Subsidiaries as of September 30, 2001. 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 Debtor.

G. Ownership. The Debtor is the legal and beneficial owner of the Collateral of the Debtor free and clear of any lien, claim, option or right of others, except for the security interest created under this Company Security Agreement, the Watson Security Agreement and the Company security agreements executed in connection with the March 1998 Debentures and the May 1999 Debentures. No effective financing statement or other instrument similar in effect covering all or any part of such Collateral or listing the Debtor or any trade name of the Debtor is on file in any recording office, except such as may have been filed relating to the Watson Loan Agreement, the March 1998 Debentures and the May 1999 Debentures. The Agent has, for the benefit of the Purchasers, a valid and perfected security interest in the Collateral, which security interest, has priority over any and all other security interests (except as otherwise provided in the Subordination Agreement) in such Collateral.

SECTION IV. COVENANTS OF THE DEBTOR.

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

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

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

D. Additional Liens; Transfers. Without the prior written consent of the Agent, the Debtor will not, in any way, hypothecate or create or permit to exist any lien, security interest, charge or encumbrance on or other interest in the Collateral, other than those permitted under the terms of the Purchase Agreement and the liens in favor of Watson pursuant to the Watson Loan Agreement and documents relative thereto[, the investors in the March 1998 Debentures and the investors in the May 1999 Debentures], and Debtor will not sell, transfer, assign, pledge, collaterally assign, exchange or otherwise dispose of the Collateral, other than the sale of Inventory in the ordinary course of business and the sale of obsolete or worn out Equipment. Notwithstanding the foregoing, if the proceeds of any such sale consist of notes, instruments, documents of title, letters of credit or chattel paper, such proceeds shall be promptly delivered to the Agent to be held as Collateral hereunder. If the Collateral, or any part thereof, is sold, transferred, assigned, exchanged, or otherwise disposed of in violation of these provisions, the security interest of the Agent shall continue in such Collateral or part thereof notwithstanding such sale, transfer, assignment, exchange or other disposition, and the Debtor will hold the proceeds thereof for the benefit of the Agent, and promptly transfer such proceeds to the Agent in kind.

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

F. Agent's Right to Protect Collateral. Upon the occurrence or continuance of an Event of Default, the Agent shall have the right at any time to make any payments and do any other acts the Agent may deem necessary to protect the security interests of the Purchasers in the Collateral, including, without limitation, the rights to pay, purchase, contest or compromise any encumbrance, charge or lien which, in the reasonable judgment of the Agent, appears to be prior to or superior to the security interests granted hereunder, and appear in and defend any action or

proceeding purporting to affect its security interests in, and/or the value of, the Collateral. The Debtor hereby agrees to reimburse the Agent for all payments made and expenses incurred under this Company Security Agreement including reasonable fees, expenses and disbursements of attorneys and paralegals acting for the Agent, including any of the foregoing payments under, or acts taken to protect its security interests in, the Collateral, which amounts shall be secured under this Company Security Agreement, and agrees it shall be bound by any payment made or act taken by the Agent hereunder absent the Agent's gross negligence or willful misconduct. The Agent shall have no obligation to make any of the foregoing payments or perform any of the foregoing acts.

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

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

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

in effect in the United States of America.

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

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

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

M. Intellectual Property. With respect to each item of its intellectual property, the Debtor agrees to take, at its expense, all necessary steps, including, without limitation, in the U.S. Patent and Trademark Office, the U.S. Copyright Office and any other governmental authority, to (i) maintain the validity and enforceability of such intellectual property and maintain such intellectual property in full force and effect, and (ii) pursue the registration and maintenance of each patent, trademark, or copyright registration or application, now or hereafter included in such intellectual property Collateral of the Debtor, including, without limitation, the payment of required fees and taxes, the filing of responses to office actions issued by the U.S. Patent and Trademark Office, the U.S. Copyright Office or other governmental authorities, the filing of applications for renewal or extension, the filing of affidavits under Sections 8 and 15 of the U.S. Trademark Act, the filing of divisional, continuation, continuation-in-part, reissue and renewal applications or extensions, the payment of maintenance fees and the participation in interference, reexamination, opposition, cancellation, infringement and misappropriation proceedings. Neither the Debtor nor the Grantor shall, without the prior written consent of the Agent, discontinue use of or otherwise abandon any intellectual property Collateral, or abandon any right to file an application for any patent, trademark or copyright, unless the Debtor shall have previously determined that such use or the pursuit or maintenance of such intellectual property is no longer desirable in the conduct of the Debtor's business and that the loss thereof would not be reasonably likely to have a Material Adverse Effect, in which case, the Debtor will give prompt notice of any such abandonment to the Agent.

N. Further Assurances. The Debtor shall take all such further actions and

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

SECTION V. REMEDIES.

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

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

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

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

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

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

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

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

(c) while the Collateral shall be so stored and kept, provide such guards and maintenance services as shall be necessary to protect the same and to preserve and maintain the Collateral in good condition;

it being understood that the Debtor's obligation to so deliver the Collateral is of the essence of this Company Security Agreement and that, accordingly, upon application to a court of

equity having jurisdiction, the Agent shall be entitled to a decree requiring specific performance by the Debtor of said obligation.

B. Disposition of the Collateral. Subject to the Subordination Agreement, any collateral repossessed by the Agent under or pursuant to Section V.A. and any other Collateral whether or not so repossessed by the Agent, may be sold, assigned, leased or otherwise disposed of under one or more contracts or as an entirety, and without the necessity of gathering at the place of sale the property to be sold, and in general in such manner, at such time or times, at such place or places and on such terms as the Agent may, in compliance with any mandatory requirements of applicable law, determine to be commercially reasonable. Any of the Collateral may be sold, leased or otherwise disposed of, in the condition in which the same existed when taken by the Agent or after any overhaul or repair which the Agent shall determine to be commercially reasonable. Any such disposition which shall be a private sale or other private proceedings permitted by such requirements shall be made upon not less than ten (10) days' written notice to the Debtor specifying the time at which such disposition is to be made and the intended sale price or other consideration therefor, and shall be subject, for the ten (10) days after the giving of such notice, to the right of the Debtor or any nominee of the Debtor to acquire the Collateral involved at a price or for such other consideration at least equal to the intended sale price or other consideration so specified. Any such disposition which shall be a public sale permitted by such requirements shall be made upon not less than ten (10) days' written notice to the Debtor specifying the time and place of such sale and, in the absence of applicable requirements of law, shall be by public auction (which may, at the option of the Agent, be subject to reserve), after publication at least once in The New York Times not less than ten (10) days prior to the date of sale. If The New York Times is not then being published, publication may be made in lieu thereof in any newspaper then being circulated in the City of New York, New York, as the Agent may elect. All requirements of reasonable notice under this Section V.B. shall be met if such notice is mailed, postage prepaid at least ten (10) days before the time of such sale or disposition, to the Debtor at its address set forth herein or such other address as the Debtor may have, in writing, provided to the Agent. The Agent may, if it deems it reasonable, postpone or adjourn any sale of any collateral from time to time by an announcement at the time and place of the sale to be so postponed or adjourned without being required to give a new notice of sale. The proceeds realized from the sale of any Collateral shall be applied as follows: first, to the reasonable costs, expenses and attorneys' fees and expenses incurred by Agent for collection and for acquisition, completion, protection, removal, storage, sale and delivery of the Collateral; second, to interest due on any of the Obligations and any fees payable under this Agreement; and third, to the principal of the Obligations. If any deficiency shall arise, Guarantors shall remain liable to Agent and Purchasers therefor.

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

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

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

(iii) give customers indebted on Accounts notice of the Agent's interest therein and/or to instruct such customers to make payment directly to the Agent for the Debtor's account;

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

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

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

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

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

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

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

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

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

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

SECTION VI. MISCELLANEOUS PROVISIONS.

A. Notices. All notices, approvals, consents or other communications required or desired to be given hereunder shall be delivered in person, by facsimile transmission followed promptly by first class mail, by a nationally recognized courier service marked for next business day delivery or by overnight mail, and delivered, if to the Agent, then to the attention of Bruce F. Wesson c/o Galen Partners III, L.P., 610 Fifth Avenue, Fifth Floor, New York, New York 10020, fax no. (212) 218-4999, with a copy to George N. Abrahams, Esq., Wolf, Block, Schorr and Solis-Cohen, 250 Park Avenue, New York, New York 10177, fax no. (212) 986-0604 and if to Debtor, then to the attention of Mr. Michael Reicher, 695 N. Perryville Road, Rockford, Illinois 61107, with a copy to John P. Reilly, Esq., St. John & Wayne, L.L.C., 2 Penn Plaza East, Newark, NJ 07105, fax no. (973) 491-3555.

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

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

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

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

F. Continuing Security Interest. This Company Security Agreement shall create a continuing security interest in the Collateral, and shall (i) remain in full force and effect until the Security Interest Termination Date, (ii) be binding upon the Debtor, and its successors and assigns and (iii) inure to the benefit of the Agent and its successors and assigns.

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

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

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

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

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

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

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

L. Release; Termination of Agreement. Subject to the provisions of Section VI.G. hereof, this Company Security Agreement shall terminate upon full and final indefeasible payment and performance of all the Obligations owing by the Debtor. At such time, the Agent shall,

at the request of the Debtor, reassign and redeliver to the Debtor all of the Collateral hereunder which has not been sold, disposed of, retained or applied by the Agent in accordance with the terms hereof. Such reassignment and redelivery shall be without warranty by or recourse to the Agent, except as to the absence of any prior assignments by the Agent of its interest in the Collateral, and shall be at the expense of the Debtor.

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

N. Governing Law. This Company Security Agreement and the rights of the parties hereunder shall be governed by, and construed in accordance with, the laws of the State of New York wherein the terms of this Company Security Agreement were negotiated, excluding to the greatest extent permitted by law any rule of law that would cause the application of the laws of any jurisdiction other than the State of New York.

O. SUBMISSION TO JURISDICTION.

(i) Each of the parties hereto hereby irrevocably and unconditionally submits, for itself and its property, to the nonexclusive jurisdiction of any New York State court or United States Federal court sitting in New York City, and any appellate court from any thereof, in any action or proceeding arising our of or relating to this Company Security Agreement or any of the other Transaction Documents (as such term is defined in the Purchase Agreement) (the "Transaction Documents") to which it is a party, or for recognition or enforcement of any judgment, and each of the parties hereto irrevocably and unconditionally agrees that all claims in respect of any such action or proceeding may be heard and determined in any such New York State court or, to the fullest extent permitted by law, in such United States Federal court. Each of the parties hereto agrees that a final judgment in any such action or proceeding shall be conclusive and may be enforced in other jurisdictions by suit on the right that any party may otherwise have to bring any action or proceeding relating to this Company Security Agreement or any of the other Transaction Documents in the courts of any other jurisdiction.

(ii) Each of the parties hereto irrevocably and unconditionally waives, to the fullest extent it may legally and effectively do so, any objection that it may now or hereafter have to the laying of venue of any suit, action or proceeding arising out of or in relation to this Company Security Agreement or any other Transaction Document to which it is a party in any such New York State or United States Federal court sitting in New York City. Each of the parties hereto hereby irrevocably waives, to the fullest extent permitted by law, the defense of an inconvenient forum to the maintenance of such action or proceeding in any such court.

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

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

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

S. JURY TRIAL. EACH OF THE DEBTOR AND THE AGENT HEREBY IRREVOCABLY WAIVES ALL RIGHT TO TRIAL BY JURY IN ANY ACTION, PROCEEDING OR COUNTERCLAIM (WHETHER BASED ON CONTRACT, TORT OR OTHERWISE) ARISING OUT OF OR RELATING TO ANY TRANSACTION DOCUMENT OR THE ACTIONS OF ANY PARTY IN THE NEGOTIATION, ADMINISTRATION, PERFORMANCE OR ENFORCEMENT THEREOF.

T. Subject to Subordination Agreement. Notwithstanding anything to the contrary contained herein, the rights and remedies of the Agent and the Purchasers, and the obligations of the Debtor, under this Company Security Agreement are subject to the Subordination Agreement, as it may be amended, supplemented or otherwise modified from time to time.

[SIGNATURE PAGE TO FOLLOW]

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

HALSEY DRUG CO., INC.

By:_____
Name:
Title:

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

GALEN PARTNERS III, L.P.

By:_____
Name:
Title:

SCHEDULE A

IIIA PLACES OF BUSINESS

1. 695 N. Perryville Road, Rockford, Illinois 61107
2. 77 Brenner Drive, Congers, New York
3. 125 Wells Avenue, Congers, New York

EXHIBIT 10.3

CONTINUING UNCONDITIONAL SECURED GUARANTY
BY
HOUBA INC.

WHEREAS, HALSEY DRUG CO., INC., a New York corporation (the "Borrower"), entered into a Debenture Purchase Agreement dated as of December 20, 2002 (as amended through the date hereof, the "Purchase Agreement"; terms used herein and not otherwise defined shall have the meanings given to them in the Purchase Agreement) with the Purchasers listed on Exhibit A thereto (each a "Lender" and collectively, the "Lenders");

WHEREAS, pursuant to the Purchase Agreement, the Lenders have made financial accommodations to the Borrower in accordance with the terms of the Purchase Agreement;

WHEREAS, Houba Inc. (the "Guarantor") will continue to receive certain benefits from the accommodations hereinabove described and is therefore willing to guaranty the prompt payment and performance of the obligations of the Borrower, on the terms set forth in this Continuing Unconditional Secured Guaranty ("Guaranty");

WHEREAS, pursuant to the Purchase Agreement, the Lenders have required that the Guarantor execute and deliver this Guaranty to Galen Partners III, L.P., a Delaware limited partnership, acting in its capacity as agent for the Lenders (the "Agent"), for the benefit of the Lenders, as a condition to the effectiveness of the Purchase Agreement; and

WHEREAS, the extension of credit by the Lenders to the Borrower is necessary and desirable to the conduct and operation of the business of the Borrower and will inure to the financial benefit of the Guarantor.

NOW, THEREFORE, for value received and in consideration of any loan, advance, or financial accommodation of any kind whatsoever heretofore, now or hereafter made, given or granted to the Borrower by the Lenders (including, without limitation, the loans evidenced by the Debenture as made by the Lenders to the Borrower pursuant to, the Purchase Agreement) and other good and valuable consideration (the sufficiency and receipt of which are hereby acknowledged), the Guarantor unconditionally guarantees to the Agent for the benefit of the Lenders (i) the full and prompt payment and performance when due, whether at maturity or earlier, by reason of acceleration or otherwise, and at all times thereafter, of all liabilities of the Borrower to the Lenders and (ii) the prompt, full and faithful discharge by the Borrower of each and every term, condition, agreement, representation, warranty or covenant now or hereafter made by the Borrower to the Lenders, in each case, and the Agent under these clauses (i) and (ii), pursuant to the Purchase Agreement, the Debentures, the other Transaction Documents (as defined in the Subordination Agreement) or any document or instrument delivered by the Borrower to the Lenders in connection therewith or pursuant thereto (which, together with the liabilities described in clause (i) hereof, are collectively referred to herein as the "Borrower's Liabilities"). The Guarantor further agrees to pay all reasonable out-of-pocket costs and expenses, including, without limitation, all court costs and reasonable attorneys' and paralegals' fees paid or incurred by the Lenders and the Agent (on behalf of the Lenders),

in endeavoring to collect all or any part of the Borrower's Liabilities from, or in prosecuting any action against the Guarantor or any other guarantor of all or any part of the Borrower's Liabilities.

Notwithstanding any provision of this Guaranty to the contrary, it is intended that this Guaranty, and any liens and security interests granted by the Guarantor to secure this Guaranty, not constitute a Fraudulent Conveyance (as defined below). Consequently, the Guarantor agrees that if this Guaranty, or any liens or security interests securing this Guaranty, would, but for the application of this sentence, constitute a Fraudulent Conveyance, this Guaranty and each such lien and security interest shall be valid and enforceable only to the maximum extent that would not cause this Guaranty or such lien or security interest to constitute a Fraudulent Conveyance, and this Guaranty shall automatically be deemed to have been amended accordingly at all relevant times. For purposes hereof, "Fraudulent Conveyance" means a transfer of property or the incurrence of liability which would be avoidable under Section 548 or 544(b) of the "Bankruptcy Code" (as hereinafter defined) or under the provisions of any applicable fraudulent conveyance or fraudulent transfer law or similar law of any state, nation or other governmental unit, as in effect from time to time.

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

The Guarantor hereby waives diligence, presentment, demand of payment, filing of claims with a court in the event of receivership or bankruptcy of the Borrower, protest or notice with respect to the Borrower's Liabilities and all demands whatsoever, and covenants that this Guaranty will not be discharged, except by complete performance of the obligations and liabilities contained herein. Upon the occurrence and during the continuance of an Event of Default under the Purchase Agreement, Lenders holding a majority in outstanding principal amount of the Debentures may, at their sole election, proceed directly and at once, without notice, against the Guarantor to collect and recover the full amount or any portion of the Borrower's Liabilities, without first proceeding against

any other person, firm, or corporation, or against any security or collateral for the Borrower's Liabilities.

The Guarantor hereby unconditionally and irrevocably agrees not to exercise any rights that it may now have or hereafter acquire against the Borrower or any other insider guarantor that arise from the existence, payment, performance or enforcement of the Borrower's Liabilities under or in respect of this Guaranty, the Purchase Agreement, the Debentures, the other Transaction Documents or any document or instrument delivered by the Borrower to the Lenders in connection therewith or pursuant thereto, including, without limitation, any right of subrogation, reimbursement, exoneration, contribution or indemnification and any right to participate in any claim or remedy of the Agent or the Lenders against the Borrower or any other insider guarantor or any Collateral, whether or not such claim, remedy or right arises in equity or under contract, statute or common law, including, without limitation, the right to take or receive from the Borrower or any other insider guarantor, directly or indirectly, in cash or other property or by set-off or in any other manner, payment or security on account of such claim, remedy or right, unless and until the Security Interest Termination Date. If any amount shall be paid to any Guarantor in violation of the immediately preceding sentence at any time prior to the indefeasible payment in full in cash of the Borrower's Liabilities and all other amounts payable under this Guaranty, such amount shall be received and held in trust for the benefit of the Lenders, shall be segregated from other property and funds of the Guarantor and shall forthwith be paid or delivered to the Agent in the same form as so received (with any necessary endorsement or assignment) to be credited and applied to the Borrower's Liabilities and all other amounts payable under this Guaranty, whether matured or unmatured, in accordance with the terms of the Debentures and the Purchase Agreement, or to be held as collateral for any Borrower's Liabilities or other amounts payable under this Guaranty thereafter arising. Upon the Security Interest Termination Date, except in the case of a Reinstatement Event (as defined below), the Agent and the Lenders will, at the Guarantor's request and expense, execute and deliver to the Guarantor appropriate documents, without recourse and without representation or warranty, necessary to evidence the transfer by subrogation to the Guarantor of an interest in the Borrower's Liabilities resulting from such payment made by the Guarantor pursuant to this Guaranty.

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

applied, reversed and reapplied, in whole or in part, to any of the Borrower's Liabilities as the Lenders shall determine in their sole discretion without affecting the validity or enforceability of this Guaranty (unless otherwise required pursuant to the Purchase Agreement).

The Guarantor hereby assumes responsibility for keeping itself informed of the financial condition of the Borrower, and any and all endorsers and/or other guarantors of any instrument or document evidencing all or any part of the Borrower's Liabilities and of all other circumstances bearing upon the risk of nonpayment of the Borrower's Liabilities or any part thereof that diligent inquiry would reveal and the Guarantor hereby agrees that neither the Agent nor the Lenders shall have any duty to advise the Guarantor of information known to any of them regarding such condition or any such circumstances or to undertake any investigation not a part of their respective regular business routines. If the Agent or any Lender, in their respective sole discretions, undertake at any time or from time to time to provide any such information to the Guarantor, the Agent or such Lender, as the case may be, shall not be under any obligation to update any such information or to provide any such information to the Guarantor on any subsequent occasion.

The Guarantor consents and agrees that neither the Agent nor the Lenders shall be under any obligation to marshall any assets in favor of the Guarantor or against or in payment of any or all of the Borrower's Liabilities. The Guarantor further agrees that, to the extent that the Borrower makes a payment or payments to the Lenders or the Lenders receive any proceeds of collateral, which payment or payments or any part thereof are subsequently invalidated, declared to be fraudulent or preferential, set aside and/or required to be repaid to the Borrower, its estate, trustee, receiver or any other party, including, without limitation, the Guarantor, under any bankruptcy law or state or federal statutory or common law, then to the extent of such payment or repayment, the Borrower's Liabilities or the part thereof which has been paid, reduced or satisfied by such amount, and the Guarantor's obligations hereunder with respect to such portion of the Borrower's Liabilities, shall be reinstated and continued in full force and effect as of the date such initial payment, reduction or satisfaction occurred. Notwithstanding anything else to the contrary contained herein, the Guarantor consents and agrees that this Guaranty shall continue to be effective or be reinstated, as the case may be, if at any time any payment of any of the Borrower's Liabilities is rescinded or must otherwise be returned by any Lender or any other Person upon the insolvency, bankruptcy or reorganization of the Borrower or the Guarantor or otherwise, all as though such payment had not been made (each such continuation or reinstatement, a "Reinstatement Event").

Until the Security Interest Termination Date, the Guarantor hereby waives any and all claims (including, without limitation, any claim for reimbursement, contribution or subrogation) of the Guarantor against the Borrower, any endorser or any other guarantor of all or any part of the Borrower's Liabilities, or against any of the Borrower's properties, arising by reason of any payment by the Guarantor to the Lenders pursuant to the provisions hereof.

Each Lender may, to the extent and in the manner set forth in the Purchase Agreement, sell or assign the Borrower's Liabilities or any part thereof, or grant participations therein, and in any such event each and every permitted assignee or holder of, or participant in, all or any of the Borrower's Liabilities shall have the right to enforce this Guaranty, by suit or otherwise

for the benefit of such assignee, holder, or participant, as fully as if herein by name specifically given such right.

The Guarantor hereby represents and warrants that: (a) it is a corporation duly organized, validly existing and in good standing under the laws of the State of Indiana; (b) it is duly authorized and empowered to execute and deliver this Guaranty; (c) all corporate action on the part of the Guarantor requisite for the due execution and delivery of this Guaranty and the due granting and creation of the security interests referred to herein has been duly and effectively taken; (d) the Guarantor's chief executive office is located at 695 North Perryville Road, Rockford, Illinois 61107 and (e) execution, delivery and performance of this Guaranty will not result in any violation of, conflict with, or result in a breach of, any of the terms of, or constitute a default under, any agreements, contracts, court orders or consent decrees, the Certificate of Incorporation or the By-laws, as amended, of the Guarantor.

This Guaranty shall be binding upon the Guarantor and upon the successors (including without limitation, any receiver, trustee or debtor in possession of or for the Guarantor) of the Guarantor and shall inure to the benefit of the Lenders and their respective successors and permitted assigns. Notwithstanding anything contained herein to the contrary, this Guaranty may not be assigned by the Guarantor without the prior written consent of the Lenders.

This Guaranty shall continue in full force and effect, and the Lenders shall be entitled to make loans and advances and extend financial accommodations to the Borrower on the faith hereof, until the Security Interest Termination Date and the Purchase Agreement has been terminated and the Debentures canceled. The Guarantor hereby unconditionally and irrevocably waives any right to revoke this Guaranty and acknowledges that this Guaranty is continuing in nature and applies to all Borrower's Liabilities, whether existing now or in the future.

Notwithstanding anything to the contrary contained herein, the rights and remedies of the Agent and the Lenders, and the obligations of the Guarantors, under this Guaranty are subject to the Subordination Agreement, as it may be amended, supplemented or otherwise modified from time to time.

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

THIS GUARANTY SHALL BE GOVERNED BY, AND CONSTRUED IN ACCORDANCE WITH, THE LAWS OF THE STATE OF NEW YORK WHEREIN THE TERMS OF THIS GUARANTY WERE NEGOTIATED, EXCLUDING TO THE GREATEST EXTENT PERMITTED BY LAW ANY RULE OF LAW THAT WOULD CAUSE THE APPLICATION OF ANY JURISDICTION OTHER THAN THE STATE OF NEW YORK.

The Guarantor hereby irrevocably and unconditionally submits, for itself and its

property, to the nonexclusive jurisdiction of any New York State court or United States Federal court sitting in New York City, and any appellate court from any thereof, in any action or proceeding arising our of or relating to this Guaranty or any of the other Transaction Documents (as such term is defined in the Purchase Agreement) (the "Transaction Documents") to which it is a party, or for recognition or enforcement of any judgment, and each of the parties hereto irrevocably and unconditionally agrees that all claims in respect of any such action or proceeding may be heard and determined in any such New York State court or, to the fullest extent permitted by law, in such United States Federal court. The Guarantor agrees that a final judgment in any such action or proceeding shall be conclusive and may be enforced in other jurisdictions by suit on the right that any party may otherwise have to bring any action or proceeding relating to this Guaranty or any of the other Transaction Documents in the courts of any other jurisdiction.

The Guarantor irrevocably and unconditionally waives, to the fullest extent it may legally and effectively do so, any objection that it may now or hereafter have to the laying of venue of any suit, action or proceeding arising out of or in relation to this Guaranty or any other Transaction Document to which it is a party in any such New York State or United States Federal court sitting in New York City. The Guarantor hereby irrevocably waives, to the fullest extent permitted by law, the defense of an inconvenient forum to the maintenance of such action or proceeding in any such court.

EACH OF THE PARTIES HERETO HEREBY IRREVOCABLY WAIVES ALL RIGHT TO TRIAL BY JURY IN ANY ACTION, PROCEEDING OR COUNTERCLAIM (WHETHER BASED ON CONTRACT, TORT OR OTHERWISE) ARISING OUT OF OR RELATING TO ANY TRANSACTION DOCUMENT OR THE ACTIONS OF ANY PARTY IN THE NEGOTIATION, ADMINISTRATION, PERFORMANCE OR ENFORCEMENT THEREOF.

[SIGNATURE PAGE TO FOLLOW]

IN WITNESS WHEREOF, this Guaranty has been duly executed by the undersigned as of this 20th day of December, 2002.

HOUBA, INC.

By:_____
Name:
Title:

EXHIBIT 10.4

GUARANTORS GENERAL SECURITY AGREEMENT

THIS GUARANTORS GENERAL SECURITY AGREEMENT ("Guarantors Security Agreement") is made and entered into as of December 20, 2002, among Houba, Inc. ("Houba"), an Indiana corporation, with its principal place of business at 16235 State Road 17, Culver, Indiana 46511, Halsey Pharmaceuticals, Inc. ("HPI"), a Delaware corporation, with its principal place of business at 695 North Perryville Road, Rockford, Illinois 61107 (Houba and HPI are each hereinafter referred to as a "Guarantor" and both of which are collectively referred to as the "Guarantors"), and Galen Partners III, L.P., a Delaware limited partnership, with its principal place of business at 610 Fifth Avenue, Fifth Floor, New York, New York 10020 ("Galen" or "Agent"), acting in its capacity as agent for the Purchasers (in such capacity, the "Agent") for the benefit of the Purchasers.

W I T N E S S E T H

WHEREAS, Galen, certain other purchasers (together with Galen, the "Purchasers") and Halsey Drug Co., Inc. (the "Company") have entered into a Debenture Purchase Agreement dated as of the date hereof (as the same may be amended, modified, supplemented or restated from time to time, the "Purchase Agreement"; terms which are capitalized herein and not otherwise defined shall have the meanings ascribed to them in the Purchase Agreement);

WHEREAS, each of the Guarantors has executed and delivered to the Purchasers a Continuing Unconditional Secured Guaranty dated the date hereof (each a "Guaranty") of the Company's obligations under the Purchase Agreement (collectively, the "Obligations"); and

WHEREAS, the Purchasers have required, as a condition precedent to the effectiveness of the Purchase Agreement, that each Guarantor (i) grant to the Agent, for the ratable benefit of the Purchasers, a security interest in and to the Collateral (as defined in Section II below) and (ii) execute and deliver this Guarantors Security Agreement in order to secure the payment and performance by such Guarantor of the Guaranty.

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

SECTION I. CREATION OF SECURITY INTEREST.

A. Security Interest. Each Guarantor hereby pledges, assigns and grants to the Agent a continuing perfected lien and security interest having priority over any and all other security interest (except as otherwise provided in the Subordination Agreement), in all of such Guarantor's right, title and interest in and to the Collateral (as defined in Section II below) in order to secure the payment and performance of all Obligations owing by such Guarantor.

B. Guarantors Remains Liable. Anything herein to the contrary notwithstanding, (i) the Guarantors shall remain liable under the contracts and agreements included in the Guarantors' Collateral to the extent set forth therein to perform all of their duties and obligations thereunder to the same extent as if this Guarantors General Security Agreement had not been executed, (ii) the exercise by the Agent of any of the rights hereunder shall not release the Guarantors from any of their duties or obligations under the contracts and agreements included in the Collateral and (iii) neither the Agent nor any Purchaser shall have any obligation or liability under the contracts and agreements included in the Collateral by reason of this Guarantors Security Agreement, the Purchase Agreement or any other Transaction Document, nor shall the Agent or any Purchaser be obligated to perform any of the obligations or duties of the Guarantors thereunder or to take any action to collect or enforce any claim for payment assigned hereunder.

SECTION II. COLLATERAL.

For purposes of this Guarantors Security Agreement, the term "Collateral" shall mean, with respect to each Guarantor, all of the kinds and types of property described in subsections A. through E. of this Section II, whether now owned or hereafter at any time arising, acquired or created by such Guarantor and wherever located, and includes all replacements, additions, accessions, substitutions, repairs, proceeds and products relating thereto or therefrom, and all documents, ledger sheets and files of such Guarantor relating thereto and all Proceeds of Collateral. "Proceeds" hereunder include (i) whatever is now or hereafter received by such Guarantor upon the sale, exchange, collection or other disposition of any item of Collateral, whether such proceeds constitute inventory, accounts, accounts receivable, general intangibles, instruments, securities (including, without limitation, United States of America Treasury Bills), credits, claims, demands, documents, letters of credit and letter of credit proceeds, chattel paper, documents of title, certificates of title, certificates of deposit, warehouse receipts, bills of lading, leases, deposit accounts, money, tax refund claims, contract rights, royalties, goods, equipment, payment under insurance (whether or not the Agent is the loss payee thereof, or any indemnities, warranties or guaranties, payable by reason of loss or damage to or otherwise with respect to any or the foregoing Collateral, and (ii) any such items which are now or hereafter acquired by such Guarantor with any proceeds of Collateral hereunder.

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

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

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

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

E. Intellectual Property. All of each Guarantor's intellectual property, including, without limitation, New Drug Applications, Investigatory New Drug Applications, Abbreviated New Drug Applications, Alternative New Drug Applications, registrations and quotas as issued by the Drug Enforcement Administration and/or the Attorney General of the United States pursuant to the Controlled Substances Act, certifications, permits and approvals of federal and state governmental agencies, patents, patent applications, trademarks, trademark applications, service marks, service mark applications, trade names, domain names, technical knowledge and processes, formal or informal licensing arrangements which are permitted to be assigned or pledged, blueprints, technical specifications, computer software, programs, databases, copyrights, copyright applications and all confidential and proprietary information, including, without limitation, know-how, trade secrets, manufacturing and production processes and techniques, inventions, research and development information, databases and data, including, without limitation, technical data, financial and marketing and business data, pricing and cost information and business and marketing plans, and all embodiments thereof, and rights thereto, including, without limitation, all of such Guarantor' rights to use the patents, trademarks, copyrights, service marks, or other property of the aforesaid nature of other Persons now or hereafter licensed to such Guarantor, together with the goodwill of the business symbolized by or connected with such Guarantor's trademarks, copyrights, service marks, licenses and the other rights included in this Section II(E).

F. Distributions. All interest, dividends, distributions, cash, instruments and other property from time to time received, receivable or otherwise distributed in respect of or in exchange for any or all of the then existing Collateral.

SECTION III. THE GUARANTORS' REPRESENTATIONS AND WARRANTIES.

Each Guarantor severally represents and warrants as follows:

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

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

C. Restrictions on Collateral Disposition. None of the Collateral is subject to contractual obligations that may restrict or inhibit the Agent's rights or ability to sell or dispose of the Collateral or any part thereof after the occurrence of an Event of Default except (i) the rights of Watson under the Watson Loan Agreement and the documents executed in connection therewith, including, without limitation, the Watson Security Agreement dated as of March 29, 2000 (the "Watson Security Agreement"); (ii) the rights of the investors in the 5% convertible senior secured debentures due March 31, 2006 issued pursuant to a certain Debenture and Warrant Purchase Agreement dated March 10, 1998, as amended, between the Company and the purchasers listed on the signature page thereto (the "March 1998 Debentures"); and (iii) the rights of the investors in the 5% convertible senior secured debentures due March 31, 2006 issued pursuant to certain Debenture and Warrant Purchase Agreement dated May 26, 1999, as amended, between the Company and the purchasers listed on the signature page thereto (the "May 1999 Debentures").

D. Status of Accounts. Status of Accounts. Each Account is based on an actual and bona fide rendition of services or sale of goods/products to customers, made by such Guarantor in the ordinary course of its business; the Accounts created are its exclusive property and are not and shall not be subject to any lien, consignment arrangement, encumbrance, security interest or financing statement whatsoever, except (i) the lien in favor of Watson under the Watson Loan Agreement and the documents executed in connection therewith, including, without limitation, the Watson Security Agreement, (ii) the lien in favor of the investors in the March 1998 Debentures and (iii) the lien in favor of the investors in the May 1999 Debentures, and to the best knowledge of such Guarantor, such Guarantor's customers have accepted the goods/products and services, and owe and are obligated to pay the full amounts stated in the invoices according to their terms, without any dispute, offset, defense or counterclaim.

E. Copyrights, Trademarks and Patents.

(i) Each of the Guarantors owns outright all of the Intellectual Property Rights listed on Section 4.12 of the Schedule of Exceptions attached to the Purchase Agreement 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.

(ii) Each of the Guarantors has not licensed to anyone the use of 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 of third parties.

(iii) Each of the Guarantors has no knowledge, nor has it received any notice (a) 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 (b) that the Intellectual Property Rights infringe upon the rights of any third party.

(iv) Each of the Guarantors has made or performed all filings, recordings and other acts and has paid all required fees and taxes to maintain and protect its interest in each and every item of intellectual property in full force and effect throughout the world, and to protect and maintain its interest therein including, without limitation, recordations of any of its interests in patents and trademarks with the U.S. Patent and Trademark Office and in corresponding national and international patent offices, and recordation of any of its interests in any copyrights with the U.S. Copyright Office and in corresponding national and international copyright offices. Each of the Guarantors has used proper statutory notice in connection with its use of each patent, trademark and copyright.

F. Inventory. All inventory of the Guarantors 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 Guarantors and its Subsidiaries as of June 30, 2002. 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 Guarantors.

G. Ownership. Each of the Guarantors is the legal and beneficial owner of the Collateral of the Guarantors free and clear of any lien, claim, option or right of others, except for the security interest created under this Guarantors General Security Agreement, the Watson Security Agreement and the Company Security Agreements executed in connection with the March 1998 Debentures and the May 1999 Debentures. No effective financing statement or other instrument similar in effect covering all or any part of such Collateral or listing the Guarantors or any trade name of the Guarantors is on file in any recording office, except such as may have been filed relating to the Watson Loan Agreement, the March 1998 Debentures and the May 1999 Debentures. The Agent has, for the benefit of the Purchasers, a valid and perfected security interest in the Collateral which security interest has priority over any and all other security interests (except as provided in the Subordination Agreement) in such Collateral.

SECTION IV. COVENANTS OF THE GUARANTORS.

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

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

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

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

D. Additional Liens; Transfers. Without the prior written consent of the Agent, such Guarantor will not, in any way, hypothecate or create or permit to exist any lien, security interest, charge or encumbrance on or other interest in the Collateral, other than those permitted under the terms of the Purchase Agreement and the lien in favor of Watson pursuant to the Watson Loan Agreement and documents relative thereto, the investors in the March 1998 Debentures and the investors in the May 1999 Debentures, and such Guarantor will not sell, transfer, assign, pledge, collaterally assign, exchange or otherwise dispose of the Collateral, other than the sale of Inventory in the ordinary course of business and the sale of obsolete or worn out Equipment. Notwithstanding the foregoing, if the proceeds of any such sale consist of notes, instruments, documents of title, letters of credit or chattel paper, such proceeds shall be promptly delivered to the Agent to be held as Collateral hereunder. If the Collateral, or any part thereof, is sold, transferred, assigned, exchanged, or otherwise disposed of in violation of these provisions, the security interest of the Agent shall continue in such Collateral or part thereof notwithstanding such sale, transfer, assignment, exchange or other disposition, and such Guarantor will hold the proceeds thereof for the benefit of the Agent, and promptly transfer such proceeds to the Agent in kind.

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

F. Agent's Right to Protect Collateral. Upon the occurrence or continuance of an Event of Default, the Agent shall have the right at any time to make any payments and do any other acts the Agent may deem necessary to protect the security interests of the Purchasers in the Collateral, including, without limitation, the rights to pay, purchase, contest or compromise any encumbrance, charge or lien which, in the reasonable judgment of the Agent, appears to be prior to or superior to the security interests granted hereunder, and appear in and defend any action or proceeding purporting to affect its security interests in, and/or the value of, the Collateral. The Guarantors hereby jointly and severally agree to reimburse the Agent for all payments made and expenses incurred under this Guarantors Security Agreement including reasonable fees, expenses and disbursements of attorneys and paralegals acting for the Agent, including any of the foregoing payments under, or acts taken to protect its security interests in, the Collateral, which amounts shall be secured under this Guarantors Security Agreement, and agree they shall be bound by any payment made or act taken by the Agent hereunder absent the Agent's gross negligence or willful misconduct. The Agent shall have no obligation to make any of the foregoing payments or perform any of the foregoing acts.

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

H. Insurance. Such Guarantor agrees to maintain public liability insurance, third party property damage insurance and replacement value insurance on the Collateral under such policies of insurance, with such insurance companies, in such amounts and covering such risks as

are at all times satisfactory to the Agent in its commercially reasonable judgment. All policies covering the Collateral are to name the Agent as an additional insured and the loss payee in case of loss, and are to contain such other provisions as the Agent may reasonably require to fully protect the Agent's interest in the Collateral and to any payments to be made under such policies. Guarantor will provide notice to Agent prior to any change in coverage.

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

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

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

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

M. Intellectual Property. With respect to each item of its intellectual property, each of the Guarantors agrees to take, at its expense, all necessary steps, including, without limitation, in the U.S. Patent and Trademark Office, the U.S. Copyright Office and any other governmental authority, to (i) maintain the validity and enforceability of such intellectual property and maintain such intellectual property in full force and effect, and (ii) pursue the registration and maintenance of each patent, trademark, or copyright registration or application,

now or hereafter included in such intellectual property Collateral of the Guarantors, including, without limitation, the payment of required fees and taxes, the filing of responses to office actions issued by the U.S. Patent and Trademark Office, the U.S. Copyright Office or other governmental authorities, the filing of applications for renewal or extension, the filing of affidavits under Sections 8 and 15 of the U.S. Trademark Act, the filing of divisional, continuation, continuation-in-part, reissue and renewal applications or extensions, the payment of maintenance fees and the participation in interference, reexamination, opposition, cancellation, infringement and misappropriation proceedings. Neither the Guarantors nor the Grantor shall, without the prior written consent of the Agent, discontinue use of or otherwise abandon any intellectual property Collateral, or abandon any right to file an application for any patent, trademark or copyright, unless the Guarantors shall have previously determined that such use or the pursuit or maintenance of such intellectual property is no longer desirable in the conduct of the Guarantors' business and that the loss thereof would not be reasonably likely to have a Material Adverse Effect, in which case, the Guarantors will give prompt notice of any such abandonment to the Agent.

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

SECTION V. REMEDIES.

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

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

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

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

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

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

a. forthwith cause the same to be moved to the place or places so designated by the Agent and there delivered to the Agent,

b. store and keep any Collateral so delivered to the Agent at such place or places pending further action by the Agent as provided in Section V.B., and

c. while the Collateral shall be so stored and kept, provide such guards and maintenance services as shall be necessary to protect the same and to preserve and maintain the Collateral in good condition;

it being understood that any Guarantor's obligation to so deliver the Collateral is of the essence of this Guarantors Security Agreement and that, accordingly, upon application to a court of equity having jurisdiction, the Agent shall be entitled to a decree requiring specific performance by such Guarantor of said obligation.

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

published, publication may be made in lieu thereof in any newspaper then being circulated in the City of New York, New York, as the Agent may elect. All requirements of reasonable notice under this Section V.B. shall be met if such notice is mailed, postage prepaid at least ten (10) days before the time of such sale or disposition, to the Guarantor at its address set forth herein or such other address as the Guarantor may have, in writing, provided to the Agent. The Agent may, if it deems it reasonable, postpone or adjourn any sale of any collateral from time to time by an announcement at the time and place of the sale to be so postponed or adjourned without being required to give a new notice of sale. The proceeds realized from the sale of any Collateral shall be applied as follows: first, to the reasonable costs, expenses and attorneys' fees and expenses incurred by Agent for collection and for acquisition, completion, protection, removal, storage, sale and delivery of the Collateral; second, to interest due on any of the Obligations and any fees payable under this Agreement; and third, to the principal of the Obligations. If any deficiency shall arise, Guarantors shall remain liable to Agent and Purchasers therefor.

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

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

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

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

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

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

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

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

remedies granted to the Agent in this Guarantors Security Agreement. This power of attorney is coupled with an interest and is irrevocable by such Guarantor.

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

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

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

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

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

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

SECTION VI. MISCELLANEOUS PROVISIONS.

A. Notices. All notices, approvals, consents or other communications required or desired to be given hereunder shall be delivered in person, by facsimile transmission followed promptly by first class mail, by a nationally recognized courier service marked for next business day delivery or by overnight mail, and delivered if to the Agent, then to the attention of Bruce F. Wesson, c/o Galen Partners III, L.P., 610 Fifth Avenue, Fifth Floor, New York, New York 10020, fax no. (212) 218-4990, with a copy to George N. Abrahams, Esq., c/o Wolf, Block, Schorr and Solis-Cohen, 250 Park Avenue, New York, New York 10177, fax no. (212) 986-0604, and if to the Guarantors, then to c/o Halsey Drug Co., Inc., attention of Mr. Michael Reicher, 695 N. Perryville Road, Rockford, Illinois 61107, with a copy to John P. Reilly, Esq., St. John & Wayne, L.L.C., 2 Penn Plaza East, Newark, NJ 07105, fax no. (973) 491-3555.

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

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

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

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

F. Continuing Security Interest. This Guarantors General Security Agreement shall create a continuing security interest in the Collateral and shall (i) remain in full force and effect until the Security Interest Termination Date, (ii) be binding upon each Guarantor, and its successors and assigns and (iii) inure to the benefit of the Agent and its successors and assigns.

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

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

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

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

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

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

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

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

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

N. GOVERNING LAW. This Guarantors Security Agreement and the rights of the parties hereunder shall be governed by, and construed in accordance with, the laws of the State of New York wherein the terms of this Guarantors Security Agreement were negotiated, excluding to the greatest extent permitted by law any rule of law that would cause the application of the laws of any jurisdiction other than the State of New York.

O. SUBMISSION TO JURISDICTION.

(i) Each of the parties hereto hereby irrevocably and unconditionally submits, for itself and its property, to the nonexclusive jurisdiction of any New York State court or United States Federal court sitting in New York City, and any appellate court from any thereof, in any action or proceeding arising our of or relating to this Guarantors Security Agreement or any of the other Transaction Documents (as such term is defined in the Subordination Agreement) to which it is a party, or for recognition or enforcement of any judgment, and each of the parties hereto irrevocably and unconditionally agrees that all claims in respect of any such action or proceeding may be heard and determined in any such New York State court or, to the fullest extent permitted by law, in such United States Federal court. Each of the parties hereto agrees that a final judgment in any such action or proceeding shall be conclusive and may be enforced in other jurisdictions by suit on the right that any party may otherwise have to bring any action or proceeding relating to this Guarantors Security Agreement or any of the other Transaction Documents in the courts of any other jurisdiction.

(ii) Each of the parties hereto irrevocably and unconditionally waives, to the fullest extent it may legally and effectively do so, any objection that it may now or hereafter have to the laying of venue of any suit, action or proceeding arising out of or in relation to this Guarantors Security Agreement or any other Transaction Document to which it is a party in any such New York State or United States Federal court sitting in New York City. Each of the parties hereto hereby irrevocably waives, to the fullest extent permitted by law, the defense of an inconvenient forum to the maintenance of such action or proceeding in any such court.

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

Q. LIMITATION OF LIABILITY. THE AGENT SHALL NOT HAVE ANY LIABILITY TO ANY GUARANTOR (WHETHER SOUNDING IN TORT, CONTRACT, OR OTHERWISE) FOR LOSSES SUFFERED BY ANY GUARANTOR IN CONNECTION WITH, ARISING OUT OF, OR IN ANY WAY RELATED TO THE TRANSACTIONS OR RELATIONSHIPS CONTEMPLATED BY THIS GUARANTORS SECURITY AGREEMENT,

OR ANY ACT, OMISSION OR EVENT OCCURRING IN CONNECTION THEREWITH, UNLESS IT IS DETERMINED BY A FINAL AND NONAPPEALABLE JUDGMENT OR COURT ORDER BINDING ON THE AGENT, THAT THE LOSSES WERE THE RESULT OF ACTS OR OMISSIONS CONSTITUTING GROSS NEGLIGENCE OR WILLFUL MISCONDUCT.

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

S. JURY TRIAL. EACH OF THE GUARANTORS AND THE AGENT HEREBY IRREVOCABLY WAIVES ALL RIGHT TO TRIAL BY JURY IN ANY ACTION, PROCEEDING OR COUNTERCLAIM (WHETHER BASED ON CONTRACT, TORT OR OTHERWISE) ARISING OUT OF OR RELATING TO ANY TRANSACTION DOCUMENT OR THE ACTIONS OF ANY PARTY IN THE NEGOTIATION, ADMINISTRATION, PERFORMANCE OR ENFORCEMENT THEREOF.

T. Subject To Subordination Agreement. Notwithstanding anything to the contrary contained herein, the rights and remedies of agent and the purchases, and the obligations of the guarantors, under this guarantors general security agreement are subject to the subordination agreement, as it may be amended, supplemented or otherwise modified from time to time.

[SIGNATURE PAGE TO FOLLOW]

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

HOUBA, INC.

By:_____
Name:
Title:

HALSEY PHARMACEUTICALS, INC.

By:_____
Name:
Title:

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

GALEN PARTNERS III, L.P.

By:_____
Name:
Title:

SCHEDULE A

SECTION III.A

- - Houba

16235 State Road 17, Culver, Indiana 46511.

- - HPI

695 N. Perryville Road, Rockford, Illinois 61107.

STOCK PLEDGE AGREEMENT

THIS STOCK PLEDGE AGREEMENT (this "AGREEMENT") dated December 20, 2002 from HALSEY DRUG CO., INC., a New York corporation (the "PLEDGOR"), GALEN PARTNERS III, L.P., a Delaware limited partnership ("GALEN"), acting in its capacity as agent for the Purchasers, as hereinafter defined (the "AGENT" or the "PLEDGEE") for the benefit of the Purchasers.

WHEREAS, the Pledgor is entering into a Debenture Purchase Agreement dated as of December 20, 2002 (the "PURCHASE AGREEMENT") with various purchasers, including the Agent (collectively, the "PURCHASERS"); and

WHEREAS, it is a condition precedent to the effectiveness of the Purchase Agreement that the Pledgor shall have executed this Agreement and made the pledges referred to herein in favor of the Pledgee, for the ratable benefit of the Purchasers, as contemplated hereby.

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

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

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

(a) As security for the prompt payment and performance when due of the obligations owing by the Pledgor to the Purchasers under the Purchase Agreement, the Debentures, the other Transaction Documents (as defined in the Subordination Agreement) and under the agreements, documents and instruments delivered by the Pledgor pursuant thereto or in connection therewith (collectively, the "OBLIGATIONS"), the Pledgor hereby pledges to the Pledgee, for the ratable benefit of the Purchasers, and grants to the Pledgee, for the ratable benefit of the Purchasers, a lien on and security interest having priority over any and all other security interests (except as otherwise provided in the Subordination Agreement), in the following (collectively the "PLEDGED COLLATERAL"): (i) all of the issued and outstanding shares of common stock of Houba, Inc. ("HOUBA" or a "SUBSIDIARY") and Halsey Pharmaceuticals, Inc. ("HPI" or a "SUBSIDIARY" and together with Houba, the "SUBSIDIARIES") which shares are more particularly described on Schedule A attached hereto (the "PLEDGED STOCK"), (ii) all additional shares of common stock at any time issued to the Pledgor by Houba or HPI, (iii) the certificates evidencing all Pledged Collateral, (iv) subject to Section 6 hereof, all dividends, cash, securities, investment property, instruments and other property from time to time received, receivable or otherwise distributed in respect of or in exchange for any or all of the Pledged Stock and such shares and securities and (v) all proceeds of any and all Pledged Collateral

(including, without limitation, proceeds constituting any property of the types described above). The Pledgor shall deliver to the Pledgee original stock certificates for all of the Pledged Stock, each accompanied by an undated stock power executed in blank by the Pledgor.

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

(c) The Pledgor, to the fullest extent permitted by law, hereby constitutes and irrevocably appoints the Pledgee (and any officer or agent of the Pledgee, with full power of substitution and revocation) as the Pledgor's true and lawful attorney-in-fact, in the Pledgor's stead and in the name of the Pledgor or in the name of the Pledgee, to transfer, upon the occurrence and during the continuance of an Event of Default or at any time the Pledgee, based on all the facts and circumstances then existing, and in the exercise of its commercially reasonable credit judgment, reasonably believes, and has so notified the Pledgor in writing, that, in connection with the Purchase Agreement and the agreements, documents and instruments delivered by the Pledgor pursuant thereto or in connection therewith, fraud has occurred with respect to the Pledgor or any other Person (for the purposes of this Agreement, the term "Person" means any individual, corporation, limited liability company, partnership, association, trust or any other entity or organization, including a government or political subdivision or an agency or instrumentality thereof, controlling, controlled by, or under common control with the Pledgor which has a material adverse effect on the operations or condition (financial or otherwise) of the Pledgor and its subsidiaries, taken as a whole (a "FRAUD"), the Pledged Collateral on the books of Houba and HPI, as applicable, in whole or in part, to the name of the Pledgee or such other Person or Persons as the Pledgee may designate and, upon the occurrence and during the continuance of an Event of Default or at any time the Pledgee, based on all the facts and circumstances then existing, and in the exercise of its commercially reasonable credit judgment, reasonably believes, and has so notified the Pledgor in writing, that Fraud has occurred, to take all such other and further actions as the Pledgor could have taken with respect to the Pledged Collateral which the Pledgee in its reasonable judgment determines to be necessary or appropriate to accomplish the purposes of this Agreement.

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

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

writing that based on all the facts and circumstances then existing, and in the exercise of its commercially reasonable judgment, such Person reasonably believes that Fraud has occurred.

3. Rights of the Pledgor; Voting.

(a) During the term of this Agreement and subject to the Subordination Agreement, and so long as the Pledgor has not received a Voting Notice (as defined below) from the Pledgee following (i) the occurrence and during the continuance of an Event of Default or (ii) from and after such time as the Pledgee determines that based on all the facts and circumstances then existing, and in the exercise of its commercially reasonable judgment, the Pledgee reasonably believes that Fraud has occurred, the Pledgor shall have the right to vote any of the Pledged Collateral in all corporate matters except those which would contravene this Agreement, the Purchase Agreement or any of the agreements, documents and instruments delivered by the Pledgor and each Subsidiary pursuant thereto unless the Pledgee consents in writing thereto.

(b) Subject to the Subordination Agreement, upon the occurrence and during the continuance of an Event of Default or from and after such time as the Pledgee has notified the Pledgor in writing that based on all the facts and circumstances then existing, and in the exercise of its commercially reasonable judgment, Pledgee reasonably believes that Fraud has occurred, the Pledgor shall give the Pledgee at least fifteen (15) days' prior notice of (i) any meeting of stockholders of any of the Subsidiaries or any meeting of directors of any of the Subsidiaries convened for any purpose and (ii) any written consent which the Pledgor proposes to execute as the stockholder of any of the Subsidiaries or which any of the representatives of the Pledgor proposes to execute as a director of any of the Subsidiaries. Subject to the Subordination Agreement, during the continuance of an Event of Default and from and after such time as the Pledgee determines that based on all the facts and circumstances then existing, and in the exercise of its commercially reasonable judgment, the Pledgee reasonably believes that Fraud has occurred, the Pledgor hereby authorizes the Pledgee to send its agents and representatives to any such meeting of shareholders or directors of any of the Subsidiaries that the Pledgee wishes to attend, and agrees to take such steps as may be necessary to confirm and effectuate such authority, including, without limitation, causing such Subsidiary to give reasonable prior written notice to the Pledgee of the time and place of any such meeting and the principal actions to be taken thereat.

(c) Notwithstanding the occurrence of an Event of Default or the determination by the Pledgee that based on all the facts and circumstances then existing, and in the exercise of its commercially reasonable judgment, the Pledgee reasonably believes that Fraud has occurred, and subject to the Subordination Agreement, the Pledgor may continue to exercise the voting rights of the Pledgor as herein described (and subject to the limitations herein) except to the extent that the Pledgee elects to exercise voting power (as determined by it in its sole discretion) by providing written notice to the Pledgor at any time during the continuance of an Event of Default or from and after such time as the Pledgee has determined that based on all the facts and circumstances then existing, and in the exercise of its commercially reasonable judgment, the Pledgee reasonably believes that Fraud has occurred (a "VOTING NOTICE"), whereupon the Pledgee shall have the exclusive right during the continuance of an Event of Default and after the Pledgee's determination of Fraud to exercise such rights to the extent specified in such Voting Notice, and the Pledgor shall take all such steps as may be necessary to effectuate such rights until the Pledgee notifies the Pledgor

in writing of the release of such rights. Once any such Event of Default has been cured or waived and such cure or waiver is confirmed by the Pledgee to the Pledgor in writing, any relevant Voting Notice shall be deemed to be rescinded.

4. No Restrictions on Transfer. The Pledgor warrants and represents that except as provided pursuant to (a) that certain Stock Pledge Agreement dated March 10, 1998 between the Company and the investors in the March 1998 Debentures, (b) that certain Stock Pledge Agreement dated May 26, 1999 between the Company and the investors in the May 1999 Debentures and (c) that certain Stock Pledge Agreement by and between the Company and Watson, dated as of March 29, 2000, there are no restrictions on the transfer of the Pledged Stock except for such restrictions imposed by operation of law, that there are no options, warrants or rights pertaining thereto, and that the Pledgor has the right to transfer the Pledged Stock free of any encumbrances and without the consent of the creditors of the Pledgor or the consent of any of the Subsidiaries or any other Person or any governmental agency whatsoever.

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

6. Adjustments of Capital Stock; Payment and Application of Dividends. Subject to the Subordination Agreement and the Debentureholders Agreement, in the event that during the term of this Agreement any stock dividend, reclassification, readjustment or other change is declared or made in the capital structure of any Subsidiary or if any other or additional shares of stock of any Subsidiary are issued to the Pledgor, all new, substituted and additional shares or other securities issued by reason of any such change or acquisition shall immediately be delivered by the Pledgor to the Pledgee and shall be deemed to be part of the "Pledged Collateral" under the terms of this Agreement in the same manner as the shares of capital stock originally pledged hereunder. Subject to the Subordination Agreement and the Debentureholders Agreement, upon the occurrence and during the continuance of an Event of Default and from and after such time as the Pledgee determines that based on all the facts and circumstances then existing, and in the exercise of its commercially reasonable judgment, the Pledgee reasonably believes that Fraud has occurred, all cash dividends received by or payable to the Pledgor in respect of the Pledged Collateral, including any additional shares of stock or Investment Property received by the Pledgor as a result of the Pledgor's record ownership of the Pledged Stock, shall immediately be delivered by the Pledgor to the Pledgee, to be held by the Pledgee as Pledged Collateral hereunder or to be applied by the Pledgee against the Obligations. Upon the occurrence and during the continuance of an Event of Default or from and after such time as the Pledgee determines that based on all the facts and circumstances then existing, and in the exercise of its commercially reasonable judgment, the Pledgee reasonably believes that Fraud has occurred, the Pledgor will not demand and will not be entitled to receive, any cash dividends or other income, interest or property in or with respect to the Pledged Collateral, and if the

Pledgor receives any of the same, the Pledgor shall immediately deliver it to the Pledgee to be held by it and applied as provided in the preceding sentence.

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

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

9. Events of Default; Remedies.

(a) Upon the occurrence and during the continuance of any Event of Default and from and after such time as the Pledgee determines that based on all the facts and circumstances then existing, and in the exercise of its commercially reasonable judgment, the Pledgee reasonably believes that Fraud has occurred, subject to the Subordination Agreement, the Pledgee shall have and at any time may exercise with respect to the Pledged Collateral, the proceeds thereof, and any other property or money held by the Pledgee hereunder, all rights and remedies available to it under law, including, without limitation, those given, allowed or permitted to a secured party by or under the Code, and all rights and remedies provided for herein and in the Purchase Agreement.

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

(c) Because federal and state securities laws may restrict the methods of disposition of the Pledged Stock which are readily available to the Pledgee, and specifically because a public sale thereof may be impossible or impracticable by reason of certain restrictions under the Securities Act of 1933, as amended, or under applicable Blue Sky or other state securities laws as now or hereafter in effect, the Pledgor agrees that the Pledgee may from time to time attempt to sell the Pledged Stock by means of a private placement restricting the offering or sale to a limited number of prospective purchasers who meet suitability standards the Pledgee deems appropriate and who agree that they are purchasing for their own accounts for investment and not with a view to distribution, and the Pledgee's acceptance of the highest offer obtained therefrom shall be deemed to be a commercially reasonable disposition of the Pledged Stock. To the extent permitted by law, the Pledgee or its assigns may purchase all or any part of the Pledged Stock and any purchaser thereof shall thereafter hold the same absolutely free from any right or claim of any kind. To the fullest extent permitted by law, the Pledgee shall not be obligated to make any such sale pursuant to notice and may, without notice or publication, adjourn any public or private sale by announcement at the time and place fixed for the sale, and such sale may be held at any time or place to which the same may be adjourned. If any of the Pledged Stock is sold by the Pledgee upon credit or for future delivery, the Pledgee shall not be liable for the failure of the purchaser to pay for same and, in such event, the Pledgee may resell such Pledged Stock and the Pledgor shall continue to be liable to the Pledgee for the full amount of the Obligations to the extent the Pledgee does not receive full and final payment in cash therefor.

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

10. Certain Representations and Warranties. The Pledgor represents and warrants to the Pledgee that:

(a) All shares of Pledged Stock are fully paid, duly and properly issued, nonassessable and owned by the Pledgor free and clear of any lien or encumbrance of any kind whatsoever, excepting those herein granted to the Pledgee and those granted to the investors in the March 1998 Debentures, the May 1999 Debentures and Watson. The Pledged Stock constitutes all of the outstanding securities of any class or kind of all of the Subsidiaries.

(b) Except in the case of the liens granted to the investors in the March 1998 Debentures, May 1999 Debentures and Watson, no effective financing statement or other instrument similar in effect covering all or any part of the Pledged Collateral is on file in any recording office.

(c) The pledge of the Pledged Collateral pursuant to this Agreement creates a valid and perfected first-priority security interest, in accordance with and subject to the Subordination Agreement, securing the payment of the Obligations, and all filings and other actions necessary or desirable to perfect and protect such security interest having been duly made or taken.

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

(e) The Pledgor has full right, power and authority to enter into this Agreement and to grant the security interest in the Pledged Collateral made hereby, and this Agreement constitutes the legal, valid and binding obligation of the Pledgor enforceable against the Pledgor in accordance with its terms, except as the enforceability thereof may be (i) limited by bankruptcy, insolvency, reorganization, moratorium or similar laws affecting the enforceability of creditors' rights generally, and (ii) subject to general principles of equity (regardless of whether such enforceability is considered in a proceeding in equity or at law).

(f) The execution, delivery and performance by the Company of this Agreement will not result in any violation, conflict with, or result in a breach of any of the terms of, or constitute a default under, any agreements, contracts, court orders or consent decrees, the Certificates of Incorporation or the By-laws, as amended, of the Company.

11. Indemnity and Expenses.

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

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

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

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

14. Continuing Security Interest; Assignments of Secured Debt. This Agreement shall create a continuing security interest having priority over any and all security interests (except as otherwise provided in the Subordination Agreement) in the Pledged Collateral and shall (a) remain in full force and effect until the Security Interest Termination Date, (b) be binding upon the Pledgor, and the Pledgor's successors and assigns, and upon each of the Subsidiaries, and their successors and assigns, and (c) inure, together with the rights and remedies of the Pledgee and the Purchasers hereunder, to the benefit of the Pledgee, its successors and permitted assigns. Without limiting the generality of the foregoing clause (c), the Pledgee may assign or otherwise transfer all or any portion of its rights and obligations under this Agreement to any other person or entity, to the extent and in the manner provided in the Purchase Agreement and the Subordination Agreement and such other person or entity shall thereupon become vested with all the benefits in respect hereof granted to the Pledgee herein; the Pledgee shall, however, retain all of its rights and powers with respect to any part of the Pledged Collateral not transferred. Any agent or nominee of the Pledgee shall have the benefit of this Agreement as if named herein and may exercise all the rights and powers given to the Pledgee hereunder.

15. Governing Law; Suits.

(a) 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, excluding to the greatest extent permitted by law any rule of law that would cause the application of the laws of any jurisdiction other than the State of New York.

(b) Each of the parties hereto hereby irrevocably and unconditionally submits, for itself and its property, to the nonexclusive jurisdiction of any New York State court or United States Federal court sitting in New York City, and any appellate court from any thereof, in any action or proceeding arising our of or relating to this Agreement or any of the other Transaction Documents

to which it is a party, or for recognition or enforcement of any judgment, and each of the parties hereto irrevocably and unconditionally agrees that all claims in respect of any such action or proceeding may be heard and determined in any such New York State court or, to the fullest extent permitted by law, in such United States Federal court. Each of the parties hereto agrees that a final judgment in any such action or proceeding shall be conclusive and may be enforced in other jurisdictions by suit on the right that any party may otherwise have to bring any action or proceeding relating to this Agreement or any of the other Transaction Documents in the courts of any other jurisdiction.

(c) Each of the parties hereto irrevocably and unconditionally waives, to the fullest extent it may legally and effectively do so, any objection that it may now or hereafter have to the laying of venue of any suit, action or proceeding arising out of or in relation to this Agreement or any other Transaction Document to which it is a party in any such New York State or United States Federal court sitting in New York City. Each of the parties hereto hereby irrevocably waives, to the fullest extent permitted by law, the defense of an inconvenient forum to the maintenance of such action or proceeding in any such court.

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

(a) in the case of the Pledgor, to:

Halsey Drug Co., Inc.
695 N. Perryville Road
Rockford, Illinois 61107
Telecopier No.: (815) 399-9710

with copies to:

St. John & Wayne
2 Penn Plaza East
Newark, New Jersey 07105
Attention: John P. Reilly, Esq.
Telephone No.: (973) 491-3600
Telecopier No.: (973) 491-3555

(b) in the case of the Pledgee, to:

Galen Partners III, L.P.
610 Fifth Avenue, Fifth Floor
New York, NY 10020
Telecopier No.: (212) 218-4999
Attention: Bruce F. Wesson

with a copies to:

Care Capital LLC
47 Hulfish Street, Suite 310
Princeton, New Jersey 08542
Attn: David Ramsey
Telephone No.: ( ) ___- ____

Wolf, Block, Schorr & Solis-Cohen
250 Park Avenue
New York, NY 10177
Attention: George N. Abrahams, Esq.
Telephone No.: (212) 986-1116
Telecopier No.: (212) 986-0604

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

17. Severability: Entire Agreement.

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

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

(c) Notwithstanding anything to the contrary contained herein, the rights and remedies of the Pledgee, and the obligations of the Pledgor, under this Stock Pledge Agreement are subject to the Subordination Agreement, as it may be amended, supplemented or otherwise modified from time to time.

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

19. Counterparts. This Agreement may be executed in any number of counterparts, each executed counterpart constituting an original but all counterparts together constituting only one instrument.

20. Further Assurances. Pledgor and the Pledgee shall execute, in a proper and timely manner, at or after the date hereof, such additional documents and instruments as may be reasonably requested by the other parties in connection with the consummation or confirmation of the transactions contemplated by this Agreement.

21. No Assignment. This Agreement may not be assigned by the Pledgor without the prior express written consent of the Pledgee.

22. WAIVERS OF JURY TRIAL AND CONSEQUENTIAL DAMAGES. THE PLEDGOR AND, BY ITS ACCEPTANCE HEREOF, THE PLEDGEE HEREBY IRREVOCABLY WAIVE ALL RIGHT TO TRIAL BY JURY IN ANY ACTION, PROCEEDING OR COUNTERCLAIM (WHETHER BASED ON CONTRACT, TORT OR OTHERWISE) ARISING OUT OF OR RELATING TO ANY TRANSACTION DOCUMENT OR THE ACTIONS OF ANY PARTY IN THE NEGOTIATION, ADMINISTRATION, PERFORMANCE OR ENFORCEMENT THEREOF.

NEITHER THE PLEDGOR OR THE PLEDGEE, NOR ANY EMPLOYEE AGENT OR ATTORNEY OF EITHER OF THEM, SHALL BE LIABLE TO THE OTHER FOR CONSEQUENTIAL DAMAGES ARISING FROM ANY BREACH OF CONTRACT, TORT OR OTHER WRONG RELATING TO THIS AGREEMENT OR THE ESTABLISHMENT, ADMINISTRATION OR COLLECTION OF THE OBLIGATIONS, EXCEPT FOR BAD FAITH.

[SIGNATURE PAGE TO FOLLOW]

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

HALSEY DRUG CO., INC.

By:_____
Name: Michael Reicher
Title: Chief Executive Officer

Accepted and Agreed to
on December 20, 2002

GALEN PARTNERS III, L.P.
on behalf of itself and as Agent
By: Claudius, L.L.C., General Partner

By:_____
Name:
Title:

SCHEDULE A

Designation and Number of
shares of capital stock owned by Pledgor

Issuer	Certificate No.	Designation	Number of Shares
Houba, Inc.	1	Common Stock, $.01 par value	100
Halsey Pharmaceuticals, Inc.	1	Common Stock, $.01 par value	100

EXHIBIT 10.6

VOTING AGREEMENT

This VOTING AGREEMENT (this "Agreement") dated as of December 20, 2002, among the Parties signatory hereto (the "Parties").

WHEREAS, Halsey Drug Co., Inc., a New York corporation (the "Company"), has entered into the Debenture Purchase Agreement dated of even date herewith (the "Purchase Agreement"), by and among the Company, Care Capital Investments II, LP ("Care Capital"), Essex Woodlands Health Ventures ("Essex") and other signatories thereto, providing for the issuance by the Company of 5% Convertible Senior Secured Debentures due March 31, 2006 (the "2002 Debentures") in the aggregate principal amount of $35,000,000; and

WHEREAS, Care Capital and Essex will purchase $5,000,000 and $5,000,000, respectively, in principal amount of the 2002 Debentures pursuant to the terms of the Purchase Agreement; and

WHEREAS, the Company does not have enough authorized and unreserved shares of its Common Stock, $.01 par value per share (the "Common Stock") available for issuance upon the conversion of the 2002 Debentures; and

WHEREAS, the Purchase Agreement contemplates that the purchasers of the 2002 Debentures shall have the right to vote as part of a single class with all holders of the Company's common stock on an as-converted basis; provided, however, that for so long as Care Capital holds any 2002 Debentures, such voting rights shall not apply to Care Capital; and

WHEREAS, the Company desires to amend its Certificate of Incorporation to provide for (a) an increase in the number of shares of its Common Stock in order to reserve a sufficient number of shares for issuance upon the conversion of the Debenture; and (b) the as-converted voting rights to the holders of the 2002 Debentures (including the proviso set forth in the immediately preceding recital); and

WHEREAS, as additional consideration for the investment by Care Capital and Essex, the Purchase Agreement provides that so long as Care Capital and Essex remain a holder of the 2002 Debentures, the Parties desire to vote their Securities (as defined below) in such a manner so as to elect a Care Capital nominee and an Essex nominee to the Board of Directors of the Company.

NOW, THEREFORE, in consideration of the foregoing and the mutual agreements herein contained, the Parties hereto agree as follows:

1. Amendment to Company's Certificate of Incorporation. At the Company's next upcoming Annual Meeting of Shareholders, each Party hereto will vote all (x) shares of Common Stock; (y) 5% Convertible Senior Secured Debentures issued pursuant to that certain

Debenture and Warrant Purchase Agreement dated March 10, 1998 between the Company and the purchasers listed on the signature page thereto (the "1998 Debentures"), and (z) 5% Convertible Senior Secured Debentures issued pursuant to that certain Debenture and Warrant Purchase Agreement dated May 26, 1999 between the Company and the purchasers listed on the signature page thereto (the "1999 Debentures", and together with the 1998 Debentures, the "Existing Debentures") (collectively with the shares of the Company's Common Stock, issuable upon conversion of the Existing Debentures, the "Securities") then owned by such Party in favor of the following proposed amendments to the Company's Certificate of Incorporation:

(a) Increasing the number of shares of the Company's Common Stock authorized for issuance from 80,000,000 to such number as shall equal the sum of (i) the Company's issued and outstanding Common Stock, plus (ii) the number of shares of Common Stock issuable upon the conversion and exercise of the Company's outstanding convertible securities, plus (iii) the number of shares of Common Stock issuable upon conversion of the 2002 Debentures and the exercise of the Watson Warrant (as such term is defined in the Purchase Agreement), plus (iv) 50 million shares, as such sum shall be rounded up to the nearest whole five million shares; and

(b) Providing that the holders of the 2002 Debentures shall have the right to vote as part of a single class with all holders of the Common Stock of the Company on all matters to be voted on by such stockholders with each 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 2002 Debentures immediately prior to the record date relating to such vote.

2. Election of Care Capital Nominee and Essex Nominee. From the date hereof, each Party and Care Capital and Essex (each of Care Capital and Essex, and their permitted transferees and assigns, being referred to herein as a "Designating Party") agree as follows:

(a) Each Party holding Securities shall vote its Securities, and take or cause to be taken such other actions, as may be required from time to time to elect to the Board of Directors of the Company one person designated by each Designating Party. Without limiting the generality of the foregoing, at each annual meeting of the shareholders of the Company, and at each special meeting of the shareholders and debentureholders of the Company called for the purpose of electing directors of the Company, and at any time at which the shareholders and debentureholders of the Company have the right to elect directors of the Company, in each such event, each Party shall vote all Securities owned by them (or shall consent in writing in lieu of a meeting of shareholders and debentureholders of the Company, as the case may be), or take such other actions as shall be necessary, to elect the Designating Party's designee as a director of the Company in accordance with the preceding provisions of this Section 2(a);

(b) Each Party shall take all actions necessary to remove forthwith the director designated by a Designating Party when such removal is requested for any reason, with or without cause, by such Designating Party. In the case of the death, resignation or removal as herein provided of a Designating Party's designee, each Party shall vote all Securities held by it to elect another person designated by such Designating Party pursuant to Section 2(a);

(c) Each Party hereby agrees that it will not vote any of its Securities in favor of the removal of any director that shall have been designated by a Designating Party, unless the Designating Party that has designated such director shall have consented to such removal in writing.

In the event that any Party shall fail to vote the Securities held by it in accordance with Section 2(a) and (b), such Party shall, upon such failure to so vote, be deemed immediately to have granted to each Designating Party a proxy to vote its Securities solely for the election of the nominee of such Designating Party or the removal of such Designating Party's designated director, as the case may be. Such Party acknowledges that each such proxy granted hereby, including any successive proxy, if necessary, is being given to secure the performance of an obligation hereunder, is coupled with an interest, and shall be irrevocable until such obligation is performed;

(d) No Party shall grant any proxy or enter into or agree to be bound by any voting trust with respect to the Securities held by such Party, or enter into any shareholder agreement or arrangement of any kind with any person with respect to the Securities held by such person that is, in either case, inconsistent with the terms of this Agreement (whether or not such agreement and arrangement was or is with other shareholders of the Company that are or are not parties to this Agreement);

(e) The Company shall take, or cause to be taken, such actions as may be required from time to time to establish and maintain executive, audit and compensation committees of the Board of Directors, as well as such other committees of the boards of directors of the Company as the Board of Directors shall determine, having such duties and responsibilities as are customary for such committees. The designees of each Designating Party shall be, if so requested by such Designating Party in its sole discretion, a member of each such committee; and

(f) The rights and obligations provided in this Section 2 shall be applied separately for each Designating Party, with the rights of a Designating Party terminating on the date such Designating Party ceases to be a holder of the 2002 Debentures.

3. Liability. No Party who shall vote or consent or withhold consent or make a request with respect to any Securities subject to this Agreement on, to or from any matter in compliance with the terms hereof that shall, as a result of any such vote or consent or withholding of consent or making of a request, have any obligation or liability to any other Party (whether such other Party shall also vote or consent or withhold consent or make a request with respect to any Securities, then subject to this Agreement).

4. Certain Remedies. Without intending to limit the remedies available to any of the Parties, each Party agrees that damages at law will be an insufficient remedy in the event such Party violates the terms hereof or the powers granted hereunder and each of the Parties hereto further agrees that each of the other Parties hereto may apply for and have injunctive or other equitable relief in any court of competent jurisdiction to restrain the breach or threatened breach of, or otherwise specifically to enforce, any of such Party's agreements or the powers granted hereunder set forth herein.

5. Representations. Each Party represents and warrants to each other Party that this Agreement is its legal, valid and binding obligation, enforceable against such Party in accordance with its terms, and will not result in any (a) violation or breach of, or be in conflict with, each Party's respective organizational documents or material contracts, or (b) violation of any statutes, laws, rules, regulations, orders or judgments applicable to such Party.

6. Transfer of Securities. Except as otherwise set forth in the Transaction Documents (as defined in the Purchase Agreement), nothing shall prohibit or in any manner restrict any Party's ability to freely transfer, assign, convey, or otherwise dispose of or convert its Securities; provided, however, that upon the transfer, assignment, conveyance or disposition of any Securities by a Party, such transferring Party shall cause the Person to which the Securities are transferred, assigned, conveyed or otherwise disposed to agree to be bound by the terms hereof..

7. Term. This Agreement and the Parties' obligations hereunder shall continue in effect for so long as Care Capital and Essex owns any 2002 Debentures.

8. Amendment. (a) Any term of this Agreement or the powers granted hereunder may be amended and the observance of any such term or power may be waived (either generally or in a particular instance and either retroactively or prospectively) only with the written consent of Care Capital and Essex and the holders of a majority of the Securities then subject to this Agreement.

(b) This Agreement and the powers granted hereunder may be terminated only with the written consent of Care Capital, Essex and all Parties hereto.

9. Binding Effect. (a) This Agreement and the powers granted hereunder shall be binding upon, and shall inure to the benefit of, Care Capital, Essex and the Parties.

(b) Nothing in this Agreement or the powers granted hereunder shall obligate any Party hereto, in his or her capacity as an employee, officer or director of the Company or any of its subsidiaries, to take or refrain from taking any action in any such capacity or shall

otherwise affect the rights or obligations of any such party in any such capacity.

10. Notices. 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, to the address for each Party as provided on the signature pages hereto, or to such other address as any such Party shall designate in writing at the address hereinabove provided. Any such notice, demand or communication shall be deemed to have been given (a) on the date of delivery, if delivered personally, (b) on the date of facsimile transmission, receipt confirmed, (c) one business day after delivery to a nationally recognized overnight courier service, if marked for next day delivery or (d) five business days after the date of mailing, if mailed.

11. Miscellaneous. The section headings herein are inserted for convenience of reference only and shall not affect the meaning or interpretation hereof. This Agreement and the powers granted hereunder contain the entire agreement among the Parties hereto with respect to the matters contemplated herein. If for any reason any provision hereof shall be invalid, unenforceable or inoperative, the validity and effect of the other provisions hereof shall not be affected herein. This Agreement may be executed in one or more counterparts, and by the Parties hereto in separate counterparts, each of which, when so executed and delivered, shall be deemed to be an original but all of which taken together shall constitute one and the same agreement. This Agreement shall become effective as to each signatory hereto upon the execution and delivery hereof by such signatory. This Agreement and the powers granted hereunder shall be governed in all respects by the laws of the State of New York wherein the terms of this Agreement were negotiated, excluding to the greatest extent permitted by law any rule of law that would cause the application of the laws of any jurisdiction other than the State of New York.

[SIGNATURE PAGES FOLLOW]

IN WITNESS WHEREOF, each of the Parties hereto has executed this Agreement on the date first above written.

ORACLE STRATEGIC PARTNERS, L.P.
By: Oracle Strategic Capital L.L.C.,
General Partner
200 Greenwich Avenue
3rd Floor
Greenwich, CT 06830

_____
By: Joel Liffmann
Its: Authorized Agent

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

_____
By: Srini Conjeevaram
Its: General Partner

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

_____
By: Bruce F. Wesson
Its: General Partner

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

_____
By: Srini Conjeevaram
Its: General Partner

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

_____
By: Michael K. Reicher
Its: Trustee

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

_____
By: Robert W. Baird
Its: Trustee

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

_____

ACKNOWLEDGED AND CONSENTED TO
as of the date set forth above by:

ESSEX WOODLANDS HEATH VENTURES V, L.P.,
By: Essex Woodlands Heath Ventures V, L.L.C.,
its General Partner
190 South LaSalle Street
Suite 2800
Chicago IL 60603

_____
Name: Immanuel Thangaraj
Title: Managing Director

CARE CAPITAL INVESTMENTS II, LP
By: Care Capital II, LLC, General Partner
47 Hulfish Street, Suite 310
Princeton, NJ 08542

_____
By: David R. Ramsay
Its: Authorized Signatory

Consent of Spouse

The undersigned, as the spouse of the Party who is the signatory to the foregoing Voting Agreement, hereby consents to, confirms and ratifies the terms of, and powers granted pursuant to, the foregoing Voting Agreement, and agrees to be bound by all the Party's obligations under the foregoing Agreement.

_____

Spouse of_____

EXHIBIT 10.7

DEBENTUREHOLDERS AGREEMENT

THIS DEBENTUREHOLDERS AGREEMENT (this "Debentureholders Agreement") is entered into as of December 20, 2002 by and among HALSEY DRUG CO., INC., a corporation organized and existing under the laws of the State of New York ("Halsey" or the "Company"), and each of the holders of the Company's 5% Convertible Senior Secured Debentures due March 31, 2006 listed on the signature page hereto.

WHEREAS, Halsey is a party to a certain Debenture and Warrant Purchase Agreement dated as of March 10, 1998, as amended (the "1998 Purchase Agreement"), with the persons listed on the signature pages thereto and pursuant to which the Company issued certain 5% Convertible Senior Secured Debentures due March 31, 2006 (the "1998 Debentures"); and

WHEREAS, Halsey entered into a certain Debenture and Warrant Purchase Agreement dated as of May 26, 1999, as amended (the "1999 Purchase Agreement"), with the persons listed on the signature pages thereto and pursuant to which the Company issued certain 5% Convertible Senior Secured Debentures due March 31, 2006 (the "1999 Debentures" and together with the 1998 Debentures, the "Existing Debentures"); and

WHEREAS, the Company has concurrently herewith entered into a certain Debenture Purchase Agreement dated as of December __, 2002 (the "2002 Purchase Agreement"; capitalized terms used herein but not otherwise defined herein shall have the meanings ascribed thereto in the 2002 Purchase Agreement) with Care Capital, LLC, Essex Woodlands Health Ventures Fund V and those other persons listed on the signature pages thereto and pursuant to which the Company proposes to issue certain 5% Convertible Senior Secured Debentures due March 31, 2006 (the "2002 Debentures" and together with the Existing Debentures, the "Debentures"); and

WHEREAS, it is a condition to the completion of the transactions contemplated pursuant to the 2002 Purchase Agreement that the Company shall have executed this Debentureholders Agreement providing that the approval of the holders of the Debentures shall be required as a condition to the Company's completion of certain material transactions; and

WHEREAS, the Company and the holders of the Debentures desire to enter into this Agreement to provide for the approval rights of the holders of the Debentures as hereinafter provided.

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

1. DEBENTUREHOLDER APPROVAL FOR MATERIAL TRANSACTIONS.

(a) Consent of Holders of 2002 Debentures. The Company hereby covenants and agrees, that so long as any of the 2002 Debentures remain outstanding, it will not, directly or indirectly, without the prior written consent of the holders of at least sixty-six and two-thirds percent (66 2/3%) in the aggregate principal amount of the 2002 Debentures then outstanding, take, or permit to be taken, any of the following actions or complete, or permit to be taken, any of the following transactions:

(i) Any modification of the rights of the holders of the 2002 Debentures;

(ii) Any issuance of securities, or the incurrence of indebtedness, by the Company or any Guarantor which rank senior or equal in right of payment to the 2002 Debentures;

(iii) Any declaration or payment of any dividends or distributions on, or redemptions of, any securities ranking junior in priority to the 2002 Debentures, other than dividends or distributions payable in the Company's capital stock or cash interest paid to individual investors in the Existing Debentures;

(iv) (A) A merger, reorganization, consolidation or other business combination involving the Company or any Guarantor, (B) a sale, transfer, lease, license or other disposition of all or substantially all of the assets of the Company or any Guarantor or (C) any other similar extraordinary transaction involving the Company or any Guarantor, in any single transaction or a series of related transactions (the "Extraordinary Transactions"), other than any such transaction where the cash, marketable securities and other liquid consideration received by the holders of the voting stock of the Company in such transaction is at least equal to four (4) times the then applicable conversion price of the 2002 Debentures;

(v) The liquidation, dissolution, commencement of any bankruptcy or other proceeding of the type referred to in Section 12.1(j) of the 2002 Purchase Agreement, recapitalization or reorganization of the Company (in each case whether or not they constitute transactions of the type referred to in Section 1(a)(vi) below); and

(vi) Without limiting the generality of Section 1(a)(iv) above, the consummation of a strategic alliance, Extraordinary Transaction, licensing arrangement or other corporate partnering arrangement involving the issuance by the Company or any Guarantor of in excess of ten million dollars ($10,000,000) in equity securities of the Company or any Guarantor.

(b) Consent of Holders of Debentures. Without limiting in any way the approval rights granted to the holders of the 2002 Debentures in Section 1(a) above, the Company hereby covenants and agrees, that so long as any of the Debentures remain outstanding, it will not, directly or indirectly, without the prior written consent of the holders of at least sixty-six and two-thirds percent (66 2/3%) in the aggregate principal amount of the Debentures then

outstanding, take, or permit to be taken, any of the following actions or complete, or permit to be completed, any of the following transactions:

(i) Any amendment to the Company's Certificate of Incorporation;

(ii) Any declaration or payment of any dividends or distributions on, or redemptions of, the Company's capital stock, other than dividends or distributions payable in the Company's capital stock or cash interest paid to individual investors in the 2002 Debentures, the 1999 Debentures and the 1998 Debentures;

(iii) An Extraordinary Transaction; provided, however, that (I) for purposes of calculating the consent of at least sixty-six and two-thirds percent (66 2/3%) in the aggregate principal amount of the Debentures where the cash, marketable securities and other liquid consideration received by the holders of the voting stock of the Company in such Extraordinary Transaction is at least equal to four (4) times the then applicable conversion price of (a) the 2002 Debentures, the 2002 Debentures shall be excluded, (b) the 1999 Debentures, the 1999 Debentures shall be excluded, and (c) the 1998 Debentures, the 1998 Debentures shall be excluded; and (II) no prior approval or consent of the holders of the Debentures shall be required for any Extraordinary Transaction where the cash, marketable securities and other liquid consideration received by the holders of the voting stock of the Company in such Extraordinary Transaction is at least equal to four (4) times the then highest applicable conversion price of the Debentures;

(iv) The liquidation, dissolution, commencement of any bankruptcy or other proceeding of the type referred to in Section 12.1(j) of the 2002 Purchase Agreement, recapitalization or reorganization of the Company (in each case whether or not they constitute transactions of the type referred to in Section 1(b)(vii) below);

(v) Except as otherwise waived, any issuance of the Company's securities which rank senior or equal in right of payment to the Existing Debentures;

(vi) Any increase in the number of members comprising the Company's Board of Directors above eleven (11); and

(vii) Without limiting the generality of Section 1(b)(iii) above, the consummation of a strategic alliance, Extraordinary Transaction, licensing arrangement or other corporate partnering arrangement involving the issuance by the Company of in excess of ten million dollars ($10,000,000) in equity securities of the Company or any Guarantor.

2. AMENDMENT AND WAIVER. Except as otherwise provided herein, no modification, amendment or waiver of any provision of this Debentureholders Agreement shall be effective against the Company or the holders of the Debentures unless such modification, amendment or waiver is approved in writing by the Company and the holders of not less than fifty-one percent (51%) of the aggregate principal amount of the Debentures then outstanding; provided that notwithstanding the foregoing, (a) the prior written consent of each holder of the 2002 Debentures will be required to amend any payment terms of the 2002 Debentures, (b) the prior

written consent of the holders of at least sixty-six and two-thirds percent (66 2/3%) in the aggregate principal amount of the 2002 Debentures will be required to modify, amend or waive any provision of Sections 1(a), 2(a), 2(b) and 3 of this Debentureholders Agreement and (c) the prior written consent of the holders of at least sixty-six and two-thirds percent (66 2/3%) in the aggregate principal amount of the Debentures then outstanding will be required to modify, amend or waive any provision of Section 1(b) of this Debentureholders Agreement. The failure of any party to enforce any of the provisions of this Debentureholders Agreement shall in no way be construed as a waiver of such provisions and shall not affect the right of such party thereafter to enforce each and every provision of this Debentureholders Agreement in accordance with its terms.

3. TERMINATION. This Debentureholders Agreement shall terminate on the earliest to occur of (a) mutual written agreement of the parties hereto and (b) the conversion of Debentures into the Company's Common Stock, or repayment of the Debentures with accrued and unpaid interest, or combination of the foregoing, such that the aggregate outstanding principal amount of the Debentures then outstanding is less than five million dollars ($5,000,000).

4. SEVERABILITY. Whenever possible, each provision of this Agreement shall be interpreted in such manner as to be effective and valid under applicable law, but if any provision of this Debentureholders Agreement is held to be invalid, illegal or unenforceable in any respect under any applicable law or rule in any jurisdiction, such invalidity, illegality or unenforceability shall not affect any other provision or any other jurisdiction, but this Debentureholders Agreement shall be reformed, construed and enforced in such jurisdiction as if such invalid, illegal or unenforceable provision had never been contained herein.

5. ENTIRE AGREEMENT. Except as otherwise expressly set forth herein, this document, the 2002 Purchase Agreement, the 1998 Purchase Agreement, as amended pursuant to the Amendment to Debenture and Warrant Purchase Agreement dated of even date, and the 1999 Purchase Agreement, as amended pursuant to the Amendment to Debenture and Warrant Purchase Agreement dated of even date embody the complete agreement and understanding among the parties hereto with respect to the subject matter hereof and supersede and preempt any prior understandings, agreements or representations by or among the parties, written or oral, which may have related to the subject matter hereof in any way.

6. SUCCESSORS AND ASSIGNS. Except as otherwise provided herein, this Debentureholders Agreement shall bind and inure to the benefit of and be enforceable by the Company and its successors and assigns, and the holders of the Debentures and any subsequent holders of the Debentures and the respective successors and assigns of each of them, so long as they hold the Debentures.

7. COUNTERPARTS. This Debentureholders Agreement may be executed in separate counterparts each of which shall be an original and all of which taken together shall constitute one and the same agreement.

8. NOTICES. All notices, demands or other communications to be given or delivered under or by reason of the provisions of this Debentureholders Agreement will be in writing and will be deemed to have been given when delivered personally, mailed by certified or registered mail, return receipt requested and postage prepaid, or sent via a nationally recognized overnight courier, or sent via facsimile to the recipient accompanied by a certified or registered mailing. Such notices, demands or other communications will be sent to the address indicated below:

To the Company:

Halsey Drug Co., Inc.
695 N. Perryville Road
Rockford, Illinois 61107
Attn: President
Fax: 815-399-9710

If to the holders of the Debentures:

To the address provided
on the signature pages to
the 1998 Purchase Agreement,
1999 Purchase Agreement and
2002 Purchase Agreement

or such other address or to the attention of such other person as the recipient party shall have specified by prior written notice to the sending party. Any such notice, demand or communication shall be deemed to have been given (a) on the date of delivery, if delivered personally, (a) on the date of facsimile transmission, receipt confirmed, (c) one business day after delivery to a nationally recognized overnight courier service, if marked for next day delivery or (d) five business days after the date of mailing, if mailed.

9. GOVERNING LAW. This Debentureholders Agreement shall be governed by, and construed in accordance with, the laws of the State of New York wherein the terms of this Debentureholder Agreement were negotiated, excluding to the greatest extent permitted by law any rule of law that would cause the application of the laws of any jurisdiction other than the State of New York.

10. JURISDICTION. (a) Each of the parties hereto hereby irrevocably and unconditionally submits, for itself and its property, to the nonexclusive jurisdiction of any New York State court or United States Federal court sitting in New York City, and any appellate court from any thereof, in any action or proceeding arising our of or relating to this Debentureholders Agreement to which it is a party, or for recognition or enforcement of any judgment, and each of the parties hereto irrevocably and unconditionally agrees that all claims in respect of any such action or proceeding may be heard and determined in any such New York State court or, to the fullest extent permitted by law, in such United States Federal court. Each of the parties hereto agrees that a final judgment in any such action or proceeding shall be conclusive and may be enforced in other jurisdictions by suit on the right that any party may otherwise have to bring any

action or proceeding relating to this Debentureholders Agreement in the courts of any other jurisdiction.

(b) Each of the parties hereto irrevocably and unconditionally waives, to the fullest extent it may legally and effectively do so, any objection that it may now or hereafter have to the laying of venue of any suit, action or proceeding arising out of or in relation to this Debentureholders Agreement to which it is a party in any such New York State or United States Federal court sitting in New York City. Each of the parties hereto hereby irrevocably waives, to the fullest extent permitted by law, the defense of an inconvenient forum to the maintenance of such action or proceeding in any such court.

11. WAIVER OF JURY TRIAL. EACH OF THE PARTIES HERETO HEREBY IRREVOCABLY WAIVES ALL RIGHT TO TRIAL BY JURY IN ANY ACTION, PROCEEDING OR COUNTERCLAIM (WHETHER BASED ON CONTRACT, TORT OR OTHERWISE) ARISING OUT OF OR RELATING TO THIS DEBENTUREHOLDERS AGREEMENT OR THE ACTIONS OF ANY PARTY IN THE NEGOTIATION, ADMINISTRATION, PERFORMANCE OR ENFORCEMENT THEREOF.

IN WITNESS WHEREOF, the parties hereto have executed this Debentureholders Agreement as of the date first above written.

Halsey Drug Co., Inc.

By:_____

Name:_____

Title:_____

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

_____
By: Srini Conjeevaram
Its: General Partner

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

_____
By: Bruce F. Wesson
Its: General Partner

CARE CAPITAL INVESTMENTS II, LP
By: Care Capital II, LLC, General Partner
47 Hulfish Street, Suite 310
Princeton, NJ 08542

_____
By: David R. Ramsay
Its: Authorized Signatory

MICHAEL WEISBROT
1136 Rock Creek Road
Gladwyne, Pennsylvania 19035

_____

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

_____
By: Srini Conjeevaram
Its: General Partner

ESSEX WOODLANDS HEALTH
VENTURES V, L.P.
By: Essex Woodlands Health Ventures V, L.L.C.,
its General Partner
190 South LaSalle Street, Suite 2800
Chicago, IL 60603

_____
By: Immanuel Thangaraj
Its: Managing Director

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

_____

SUSAN WEISBROT
1136 Rock Creek Road
Gladwyne, Pennsylvania 19035

_____

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

_____

GEORGE E. BOUDREAU
222 Elbow Lane
Haverford, PA 19041

_____

ROGER GRIGGS
c/o Tom Jennings
7300 Turfway Road
Suite 300
Florence, KY 41042

_____

ORACLE STRATEGIC PARTNERS, L.P.
By: Oracle Strategic Capital L.L.C.,
General Partner
200 Greenwich Avenue
3rd Floor
Greenwich, CT 06830

_____
By: Joel Liffmann
Its: Authorized Agent

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

_____
By: Bruce F. Wesson
Its: General Partner

ALAN SMITH
21 Bedlow Avenue
Newport, Rhode Island 02840

_____

MICHAEL WEISBROT
1136 Rock Creek Road
Gladwyne, Pennsylvania 19035

_____

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

_____

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

_____
By: Srini Conjeevaram
Its: General Partner

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

_____
By: Srini Conjeevaram
Its: General Partner

PATRICK COYNE
800 Merion Square Road
Gladwyne, PA 19035

_____

SUSAN WEISBROT
1136 Rock Creek Road
Gladwyne, Pennsylvania 19035

_____

DENNIS ADAMS
120 Kynlyn Road
Radnor, Pennsylvania 19312

_____

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

_____

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

_____
By: Michael K. Reicher
Its: Trustee

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

_____

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

_____

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

_____
By: Connie Reicher
Its: Trustee

STEPHANIE HEITMEYER
17759 Road, Route 66
Ft. Jennings, Ohio 45844

_____

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

_____

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

_____

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

_____
By: Varshah H. Shah
Its: Custodian

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

_____
By: Varshah H. Shah
Its: Custodian

MICHAEL RAINISCH
c/o Alvin Rainisch
31 Congressional Road
Jackson, New Jersey 08527

_____

ILENE RAINISCH
c/o Alvin Rainisch
31 Congressional Road
Jackson, New Jersey 08527

_____

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

_____

By:_____
Its: Trustee

KENNETH GIMBEL
2455 Montgomery Avenue
Highland Park, Ill. 60035

_____

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

_____

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

_____

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

_____

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

_____

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

_____

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

_____

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

_____

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

_____

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

_____
By: Robert W. Baird
Its: Trustee

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

_____
By: Robert W. Baird
Its: Trustee

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

_____
By: Michael K. Reicher
Its: Trustee

EXHIBIT 10.8

HALSEY DRUG CO., INC.

AMENDMENT TO
DEBENTURE AND WARRANT PURCHASE AGREEMENT

DATED AS OF DECEMBER 20th, 2002

This Amendment to the Debenture and Warrant Purchase Agreement is made as of this 20th day of December, 2002, by and among Halsey Drug Co., Inc., a New York corporation (the "Company"), and each of the Purchasers set forth on the signature page hereto (the "Purchasers").

R E C I T A L S :

WHEREAS, pursuant to that certain Debenture and Warrant Purchase Agreement dated as of March 10, 1998 (the "Purchase Agreement") executed by the Company in favor of the Purchasers, the Company issued its 5% Convertible Senior Secured Debentures due March 15, 2003 (the "Existing Debentures"); and

WHEREAS, pursuant to a certain Debenture Purchase Agreement dated on or about December 20, 2002 (the "2002 Purchase Agreement"), proposed to be executed by the Company in favor of Care Capital LLC, Essex Woodlands Health Ventures and the other purchasers listed on the signature page thereto, the Company proposes to issue its 5% Convertible Senior Secured Debentures due March 31, 2006 (the "New Debentures");

WHEREAS, as a condition to the investment in the New Debentures to be made by the Purchasers listed in the 2002 Purchase Agreement (the "New Holders"), the New Holders have required that the Purchase Agreement be amended to (i) extend the maturity date of the Existing Debentures from March 15, 2003 to March 31, 2006, (ii) provide that the holders of the Existing Debentures have veto rights for certain material Company transactions, (iii) provide that the right of first refusal provided to the holders of the Existing Debentures be exercisable on a pro rata basis with the New Holders under the 2002 Purchase Agreement; and (iv) reduce the number of representatives designated by the holders of the Existing Debentures from three (3) to two (2) commencing with the second Annual Meeting of Shareholders following the date of this Amendment.

WHEREAS, as an inducement for the New Holders to make the investment pursuant to the 2002 Purchase Agreement, the Company and the Purchasers desire to amend the Purchase Agreement as hereinafter provided;

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

1. Capitalized terms used herein and not otherwise defined shall have the meanings provided in the Purchase Agreement.

2. Section 1.1 of the Purchase Agreement is hereby amended to delete Subsection (a) of such Section and replace same with the following:

"(a) its 5% Convertible Senior Secured Debentures due March 31, 2006 in the aggregate principal amount of $20,800,000 (the "Debentures"),"

3. The Purchase Agreement is hereby amended to provide that the maturity date of the Debentures shall be March 31, 2006 and that any reference to a maturity date of March 15, 2003 shall be deemed changed to March 31, 2006.

4. The definition of Debentures as contained in Section 1.1 of the Purchase Agreement is hereby revised to include all 5% Convertible Senior Secured Debentures having an original maturity date of March 15, 2003 issued pursuant to the Purchase Agreement, including, without limitation, all 5% Convertible Senior Secured Debentures issued by the Company to the Purchasers in satisfaction of interest payments due and payable thereunder. Exhibit A-1 to this Amendment to the Debenture and Warrant Purchase Agreement sets forth all Debentures and Warrants issued to the Purchasers pursuant to the Purchase Agreement through the date hereof.

5. Each Purchaser agrees to surrender to the Company each Debenture instrument issued to such Purchaser as described in Exhibit A-1 to this Amendment to the Debenture and Warrant Purchase Agreement against the issuance by the Company of an Amended and Restated 5% Convertible Senior Secured Debenture of like principal amount due March 31, 2006 in substantially the form attached as Exhibit B to this Amendment to Debenture and Warrant Purchase Agreement.

6. Section 9.8 of the Purchase Agreement is hereby amended to delete subsection (a) of such Section and replace same with the following:

"(a) 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 Securities, at each annual meeting of the Company's Stockholders, the Purchasers shall have the right to nominate three (3) designees to be members of the Board of Directors; provided, however, that commencing with the Company's 2004 Annual Meeting of Shareholders, the Purchasers shall have the right to nominate two (2) designees to be members of the Board of Directors."

7. A new Section 9.18 is hereby added to the Purchase Agreement as follows:

"9.18 Debentureholders Agreement. Each of the Company and the holders of the Debentures has concurrently executed the form of Debentureholders Agreement attached as Exhibit N hereto."

8. Section 12.1(c) of the Purchase Agreement is hereby deleted in its entirety and the following inserted in lieu thereof:

"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, including that certain Registration Rights Agreement dated December 20, 2002 among the Company, the Purchasers and the other parties thereto, 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 forwith 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);"

9. Article XVI of the Purchase Agreement is hereby deleted in its entirety and the following inserted in its place:

ARTICLE 16

RIGHT OF FIRST REFUSAL: ADDITIONAL INVESTMENT

16.1 Right of First Refusal. Each Holder of the Debentures, Holder of Shares (provided any Debentures remain outstanding and the Shares received upon conversion have not been sold, transferred or otherwise disposed of) (the "Common Holder"), holders of the 2002 Debentures (the "2002 Debentureholders") and holders of shares of Common Stock issued upon the conversion of the 2002 Debentures (provided any 2002 Debentures remain outstanding and the shares of Common Stock received upon conversion have not been sold, transferred or otherwise disposed of) (the "New Common Holders") shall be entitled to the following right of first refusal:

(a) Except in the case of Excluded Securities (as hereinafter defined), the Company shall not issue, sell or exchange, agree to issue, sell or exchange, or reserve or set aside for issuance, sale or exchange (i) any shares of Common Stock, (ii) any other equity security of the Company, (iii) any debt security of the Company which by its terms is convertible into or exchangeable for, with or without consideration, any equity security of the Company, (iv) any security of the Company that is a combination of debt and equity or (v) any option, warrant or other right to subscribe for, purchase or otherwise acquire any equity security or any such debt security of the Company (collectively, the "Equity Securities") unless in each case, the Company shall have first offered to sell to the holders of Debentures, the Common Holders, the 2002 Debentureholders and the New Common Holders, the Equity Securities, at a price and on such other terms as shall have been specified by the Company in writing delivered to each of the Holders of Debentures, the Common Holders, the 2002 Debentureholders and the New Common Holders (the "Offer"), which Offer by its terms shall remain open and irrevocable for a period of thirty (30) days from the date it is delivered by the Company to the Holders of Debentures, the Common Holders, the 2002 Debentureholders and the New Common Holders; provided, however, that such issuance, sale or exchange of equity securities shall result in gross proceeds to the Company (whether at the time of issuance or upon conversion, exercise, or exchange thereof) of an amount in excess of $200,000 (the "Minimum Offering Threshold"). For purposes of computing the Minimum Offering Threshold, any offering, issuance, sale or exchange of Equity Securities during any rolling 12 month period shall be aggregated.

(b) Each of the Holders of Debentures, the Common Holders, the 2002 Debentureholders and the New Common Holders shall have the right to purchase its pro rata share of the Equity Securities. The "pro rata share" of each Holder of Debentures, Common Holder, 2002 Debentureholders and the New Common Holders shall be that amount of the Equity Securities multiplied by a fraction, the numerator of which is the sum of (i) the Shares underlying the Debenture held by such person if such person is the holder of a Debenture, (ii) the number of Shares of Common Stock issued to such Common Holder upon conversion of a Debenture if such person is a Common Holder, (iii) the number of shares of Common Stock underlying the 2002 Debentures held by such person if such person is a 2002 Debentureholder and (iv) the number of shares of Common Stock issued to a 2002 Debentureholder upon conversion of a 2002 Debenture if such person is an New Common Holder, and the denominator of which is the sum of (x) the total number of shares of Common Stock underlying the Debentures issued pursuant to this Agreement and (y) the total number of shares of Common Stock underlying the 2002 Debentures.

(c) Notice of the intention of each Holder of a Debenture, Common Holder, 2002 Debentureholder or New Common Holder to accept, in whole or in part, an Offer shall be evidenced by a writing signed by such person, as the case may be and delivered to the Company prior to the end of the 30-day period commencing with the date of such Offer or, if later within ten (10) days after the delivery of giving of any written notice of a material change in such Offer, setting forth such portion (specifying number of shares, principal amount or the like) of the Equity Securities as such person elects to purchase (the "Notice of Acceptance").

(d) In the event that all Holders of Debentures, Common Holders, 2002 Debentureholders and New Common Holders do not elect to purchase all of the Equity Securities, the persons

which have provided notice of their intention to exercise the refusal rights as provided in subparagraph (c) above shall have the right to purchase, on a pro rata basis, any unsubscribed portion of the Equity Securities during a period of ten (10) days following the 30-day period provided in subparagraph (c) above. Following such additional 10-day period, in the event the Holders of the Debentures, the Common Holders, 2002 Debentureholders and the New Common Holders have not elected to purchase all of the Equity Securities, the Company shall have 90 days from the expiration of the foregoing 40-day period to sell all or any part of such Equity Securities as to which a Notice of Acceptance has not been given by any of such persons (the "Refused Securities") to any other person or persons, but only upon terms and conditions in all material respects, including without limitation, unit price and interest rates, which are no more favorable, in the aggregate, to such other person or persons or less favorable to the Company than those set forth in the Offer. Upon the closing of the sale to such other person or persons of all of the Refused Securities, which shall include payment of the purchase price to the Company in accordance with the terms of the Offer, if the Holders of Debentures, the Common Holders, the 2002 Debentureholders and the New Common Holders have timely submitted a Notice of Acceptance, it and/or they shall purchase from the Company, and the Company shall sell to the Holders of Debentures, the Common Holders, 2002 Debentureholders and the New Common Holders, as the case may be, the Equity Securities in respect of which a Notice of Acceptance was delivered to the Company, at the terms specified it the Offer. The purchase by the Holders of Debentures, Common Holders, the 2002 Debentureholders and the New Common Holders of any Equity Securities is subject in all cases to the preparation, execution and delivery by the Company and such persons of a purchase agreement and other customary documentation relating to such Equity Securities as is satisfactory in form and substance to such persons and each of their respective counsel.

(e) In each case, any Equity Securities not purchased by the Holders of Debentures, the Common Holders, the 2002 Debentureholders and the New Common Holders or by a person or persons in accordance with Section 16.1(d) hereof may not be sold or otherwise disposed of until they are again offered to such persons under the procedures specified in Section 16.1(a), (b), (c) and (d) hereof.

(f) The rights of the Holders of Debentures, the Common Holders, 2002 Debentureholders and the New Common Holders under this Section 16.1 shall not apply to the following securities (the "Excluded Securities"):

(i) Common Stock or options to purchase such Common Stock, issued to officers, employees or directors of, or consultants to, the Company, pursuant to any agreement, plan or arrangement approved by the Board of Directors of the Company;

(ii) Common Stock issued as a stock dividend or upon any stock split or other subdivision or combination of shares of Common Stock;

(iii) Common Stock issued upon conversion of the Debentures or the 1999 Debentures, or exercise of the Warrants or the warrants issued in connection with the 1999 Debentures, or Common Stock issued upon conversion of the 2002 Debentures or exercise of the warrants issued pursuant to the 2002 Purchase Agreement;

(iv) Common Stock or debentures issued in satisfaction of interest payments on the Debentures, the 1999 Debentures and the 2002 Debentures, including the issuance of Common Stock or Debentures issued in satisfaction of interest payments on Debenture instruments issued by the Company in satisfaction of the interest payments on the Debentures, the 1999 Debenture and the 2002 Debentures; or

(v) any securities issued for consideration other than cash pursuant to a merger, consolidation, acquisition, strategic alliance or similar business

combination approved by the Board of Directors and/or at the Company's Annual Meeting of Shareholders.

(g) Notwithstanding anything to the contrary contained herein, a Holder of a Debenture, a Common Holder (other than an initial Purchaser), a 2002 Debentureholders or a New Common Holder (other than an initial purchaser of a 2002 Debenture) shall not be considered as such for purposes of this Section 16.1 only, unless such person then holds Debentures or 2002 Debentures with an outstanding principal amount of at least $200,000 or shares issued upon conversion of at least $200,000 in principal of Debentures or 2002 Debentures or a combination of Debentures or 2002 Debentures and shares of Common Stock received upon conversion of the Debentures and 2002 Debentures such that the outstanding principal of the Debentures or 2002 Debentures held by such person plus the amount of principal of Debentures or 2002 Debentures converted into shares held by such person equals or exceeds $200,000."

10. Subparagraph (a) of Article XIII is hereby amended to add the following at the end of such Subparagraph:

"Notwithstanding the foregoing or anything to the contrary contained in this Article XIII, no amendment to Section 9.18 shall be valid unless the same shall be in writing and signed by the Company and the holders of at least 66 2/3% in the aggregate principal amount of the Debenture (including for purposes such calculation the principal amount of those Debentures that at such time have been converted into shares).

11. Except as amended above, the terms of the Purchase Agreement shall remain in full force and effect.

12. This Amendment to Debenture and Warrant Purchase Agreement and the rights of the parties hereunder shall be governed in all respects by laws in the State of New York wherein the terms of this Amendment were negotiated.

13. This Amendment to Debenture and Warrant Purchase Agreement may be executed in any number of counterparts, each of which shall be original, but all of which together shall constitute one instrument.

[SIGNATURE PAGES TO FOLLOW]

IN WITNESS WHEREOF, the Company and the Purchasers have caused this Amendment to be duly executed all on the day and year first above written.

HALSEY DRUG CO., INC.

By:_____
Name: Michael Reicher
Title: Chief Executive Officer

PURCHASERS

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

_____
By: Srini Conjeevaram
Its: General Partner

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

_____
By: Srini Conjeevaram
Its: General Partner

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

_____
By: Bruce F. Wesson
Its: General Partner

ALAN SMITH
21 Bedlow Avenue
Newport, Rhode Island 02840

_____

PATRICK COYNE
800 Merion Square Road
Gladwyne, PA 19035

_____

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

_____

MICHAEL WEISBROT
1136 Rock Creek Road
Gladwyne, Pennsylvania 19035

_____

SUSAN WEISBROT
1136 Rock Creek Road
Gladwyne, Pennsylvania 19035

_____

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

_____

DENNIS ADAMS
120 Kynlyn Road
Radnor, Pennsylvania 19312

_____

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

_____

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

_____

By: Michael K. Reicher
Its: Trustee

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

_____

By: Connie Reicher
Its: Trustee

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

_____

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

_____

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

_____

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

_____

By: Varshah H. Shah
Its: Custodian

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

_____

By: Varshah H. Shah
Its: Custodian

MICHAEL RAINISCH
c/o Alvin Rainisch

ILENE RAINISCH
c/o Alvin Rainisch

300 Flower Lane
Morganville, New Jersey 07751

300 Flower Lane
Morganville, New Jersey 07751

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

KENNETH GIMBEL
2455 Montgomery Avenue
Highland Park, Ill. 60035

By:_____
Its: Trustee

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

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

_____
By: Robert W. Baird
Its: Trustee

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

_____
By: Robert W. Baird
Its: Trustee

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

_____
By: Michael K. Reicher
Its: Trustee

EXHIBIT A-1

LIST OF DEBENTURE HOLDERS

EXHIBIT B

FORM OF AMENDED AND RESTATED
5% CONVERTIBLE SENIOR SECURED DEBENTURE

EXHIBIT N

DEBENTUREHOLDER AGREEMENT

EXHIBIT 10.9

HALSEY DRUG CO., INC.

AMENDMENT TO
DEBENTURE AND WARRANT PURCHASE AGREEMENT

DATED AS OF DECEMBER 20, 2002

This Amendment to the Debenture and Warrant Purchase Agreement is made as of this 20th day of December, 2002, by and among Halsey Drug Co., Inc., a New York corporation (the "Company"), and each of the Purchasers set forth on the signature page hereto (the "Purchasers").

R E C I T A L S :

WHEREAS, pursuant to that certain Debenture and Warrant Purchase Agreement dated as of May 26, 1999 (the "Purchase Agreement") executed by the Company in favor of the Purchasers, the Company issued its 5% Convertible Senior Secured Debentures due March 15, 2003 (the "Existing Debentures"); and

WHEREAS, pursuant to a certain Debenture Purchase Agreement dated on or about December 20, 2002 (the "2002 Purchase Agreement"), proposed to be executed by the Company in favor of Care Capital LLC, Essex Woodlands Health Ventures and the other purchasers listed on the signature page thereto, the Company proposes to issue its 5% Convertible Senior Secured Debentures due March 31, 2006 (the "New Debentures"); and

WHEREAS, as a condition to the investment in the New Debentures to be made by the Purchasers listed in the 2002 Purchase Agreement (the "New Holders"), the New Holders have required that the Purchase Agreement be amended to (i) extend the maturity date of the Existing Debentures from March 15, 2003 to March 31, 2006, and (ii) provide that the holders of the Existing Debentures have veto rights for certain material Company transactions; and

WHEREAS, as an inducement for the New Holders to make the investment pursuant to the 2002 Purchase Agreement, the Company and the Purchasers desire to amend the Purchase Agreement as hereinafter provided;

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

1. Capitalized terms used herein and not otherwise defined shall have the meanings provided in the Purchase Agreement.

2. Section 1.1 of the Purchase Agreement is hereby amended to delete Subsection (a) of such Section and replace same with the following:

> "(a) its 5% Convertible Senior Secured Debentures due March 31, 2006 in the aggregate principal amount of $22,862,603.04 (the "Debentures"),"

3. The Purchase Agreement is hereby amended to provide that the maturity date of the Debentures shall be March 31, 2006 and that any reference to a maturity date of March 15, 2003 shall be deemed changed to March 31, 2006.

4. The definition of Debentures as contained in Section 1.1 of the Purchase Agreement is hereby revised to include all 5% Convertible Senior Secured Debentures having an original maturity date of March 15, 2003 issued pursuant to the Purchase Agreement, including, without limitation, all 5% Convertible Senior Secured Debentures issued by the Company to the Purchasers in satisfaction of interest payments due and payable thereunder. Exhibit A-1 to this Amendment to the Debenture and Warrant Purchase Agreement sets forth all Debentures and Warrants issued to the Purchasers pursuant to the Purchase Agreement through the date hereof.

5. Each Purchaser agrees to surrender to the Company each Debenture instrument issued to such Purchaser as described in Exhibit A-1 to this Amendment to Debenture and Warrant Purchase Agreement against the issuance by the Company of an Amended and Restated 5% Convertible Senior Secured Debenture of like principal amount due March 31, 2006 in substantially the form attached as Exhibit B to this Amendment to the Debenture and Warrant Purchase Agreement.

6. A new Section 9.16 is hereby added to the Purchase Agreement as follows:

"9.16 Debentureholders Agreement. Each of the Company and the holders of the Debentures has concurrently executed the form of Debentureholders Agreement attached as Exhibit O hereto."

7. Section 12.1(c) of the Purchase Agreement is hereby deleted in its entirety and the following inserted in lieu thereof:

"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, including that certain Registration Rights Agreement dated December 20, 2002 among the Company, the Purchasers and the other parties thereto, 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 thirty-five (35) days after a Default Notice shall have been given to the Company (the Company to give forwith 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);"

8. Subparagraph (a) of Article XIII is hereby amended to add the following at the end of such Subparagraph:

"Notwithstanding the foregoing or anything to the contrary contained in this Article XIII, no amendment to Section 9.16 shall be valid unless the same shall be in writing and signed by the Company and the holders of at least 66 2/3% in the aggregate principal amount of the Debentures (including for purposes of such calculation the principal amount of those Debentures that at such time have been converted into shares).

9. Except as amended above, the terms of the Purchase Agreement shall remain in full force and effect.

10. This Amendment to Debenture and Warrant Purchase Agreement and the rights of the parties hereunder shall be governed in all respects by laws in the State of New York wherein the terms of this Amendment were negotiated.

11. This Amendment to Debenture and Warrant Purchase Agreement may be executed in any number of counterparts, each of which shall be original, but all of which together shall constitute one instrument.

[SIGNATURE PAGES TO FOLLOW]

IN WITNESS WHEREOF, the Company and the Purchasers have caused this Amendment to be duly executed all on the day and year first above written.

HALSEY DRUG CO., INC.

By:_____
Name: Michael Reicher
Title: Chief Executive Officer

PURCHASERS

ORACLE STRATEGIC PARTNERS, L.P.
By: Oracle Strategic Capital L.L.C.,
General Partner
200 Greenwich Avenue
3rd Floor
Greenwich, CT 06830

_____
By: Joel Liffmann
Its: Authorized Agent

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

_____
By: Srini Conjeevaram
Its: General Partner

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

_____
By: Bruce F. Wesson
Its: General Partner

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

_____
By: Srini Conjeevaram
Its: General Partner

ALAN SMITH
21 Bedlow Avenue
Newport, Rhode Island 02840

_____

PATRICK COYNE
800 Merion Square Road
Gladwyne, PA 19035

_____

MICHAEL WEISBROT
1136 Rock Creek Road
Gladwyne, Pennsylvania 19035

_____

SUSAN WEISBROT
1136 Rock Creek Road
Gladwyne, Pennsylvania 19035

_____

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

DENNIS ADAMS
120 Kynlyn Road
Radnor, Pennsylvania 19312

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

EXHIBIT A-1

LIST OF DEBENTUREHOLDERS

EXHIBIT B

FORM OF AMENDED AND RESTATED
5% CONVERTIBLE SENIOR SECURED DEBENTURE

EXHIBIT O

DEBENTUREHOLDER AGREEMENT

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.
AMENDED AND RESTATED
5% CONVERTIBLE SENIOR SECURED DEBENTURE
DUE MARCH 31, 2006

$_____ No. _____

December 20, 2002

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_____ or its registered assigns (the "Payee" or "Holder") upon due presentation and surrender of this Debenture, on March 31, 2006 (the "Maturity Date"), the principal amount of _____($_____) 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 March 10, 1998 among the Company and certain persons, including the Payee, as amended pursuant to that certain Amendment to Debenture and Warrant Purchase Agreement dated as of December __, 2002 among the Company and the other signatories thereto (together with the Schedules and Exhibits thereto, the "Purchase Agreement") relating to the purchase and sale of 5% Convertible Senior Secured Debentures maturing March 31, 2006 (the "Debentures") in the aggregate principal amount of $20,800,000.00 and pursuant to which Payee and others have exercised the right provided in the Purchase Agreement to purchase additional Debentures for an aggregate purchase price of $5,000,000.00. The holders of such Debentures are referred to hereinafter as the "Holders." The Payee is entitled to the benefits of 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. Capitalized terms used and not defined herein shall have the meaning provided in the Purchase Agreement.

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) shall accrue on the unpaid portion of said principal amount from time to time outstanding at the rate of five percent (5%) per annum (the "Stated Interest Rate"), in like coin and currency, and shall be paid by the Company to the Payee at three (3) month intervals on each January 1, April 1, July 1 and October 1 during the term of this Debenture (commencing July 1, 1998) (each being an "Interest Payment Date") and on the Maturity Date. Both principal hereof and interest thereon are payable at the Holder's address as provided in the Purchase Agreement 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 address as provided in the Purchase Agreement 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 Notwithstanding anything to the contrary contained herein, including, without limitation, Section 1.1 hereof, this Amended and Restated 5% Convertible Senior Secured Debenture shall in no way terminate, modify, or otherwise waive any irrevocable election executed by such Holder and delivered to the Company providing for the Company's payment, and such Holder's acceptance, of any and all interest payments due under this Debenture in the form of like debentures of the Company in full satisfaction of the Company's interest payment obligations hereunder.

1.3 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 or otherwise shall be due and payable at the rate of seven (7%) percent per annum, subject to the limitations of applicable law.

1.4 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 March 10, 1998 and collateral assignments referred to in the Purchase Agreement. In addition, each of Houba, Inc. ("Houba"), Halsey

Pharmaceuticals, Inc., Indiana Fine Chemicals Corporation and Cenci Powder Products, Inc. ("CPP"), each a wholly-owned subsidiary of the Company, and H.R. Cenci Laboratories, Inc. ("HR Cenci"), a 97% owned subsidiary of the Company (collectively, the "Guarantors"), has executed in favor of the Holder a certain Continuing Unconditional Guaranty, dated as of March 10, 1998, 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 a "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 dated March 10, 1998 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. The obligations of each of CPP and HR Cenci under their Guaranties are also secured pursuant to a Mortgage on real property located at 152 North Broadway, Fresno, California. The rights of the Holders with respect to the collateral described in the security agreements and collateral assignments with the Company and the Guarantors as provided in the Purchase Agreement are subject to the terms of the Subordination Agreement dated of even date by and among the Company, Watson Pharmaceuticals, Inc., the Holders and the other signatories thereto.

ARTICLE III

CONVERSION

3.1 Conversion at Option of Holder. At any time and from time to time on and after as of March 10, 1998 (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 form reasonably satisfactory to the Company duly executed by the registered Holder or its duly authorized attorney. "Common Stock" of the Company means common stock of the Company as it exists on the date this Debenture is originally signed. 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"), as such conversion price may be adjusted as provided in Sections 3.5, 3.6 and 3.7 hereof (as so adjusted). 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 of Common Stock 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 in the principal amount equal to the remaining principal balance of this Debenture after giving effect to such partial conversion.

3.2 Conversion at Option of the Company. So long as an Event of Default as provided in Section 12.1(a) of the Purchase Agreement (concerning the Company's failure to pay principal and interest under the Debentures) shall not have occurred and then be continuing, in the event that either (a) following the second anniversary of March 10, 1998, the closing price per share of the Company's Common Stock on the American Stock Exchange ("AMEX") or the NASDAQ National Market ("NNM") exceeds $4.75 per share for each of twenty (20) consecutive trading days or (b) following the third anniversary of March 10, 1998, the

closing price per share of the Company's Common Stock on the AMEX or NNM exceeds $7.125 per share for each of twenty (20) consecutive trading days, then at any time thereafter until the earlier of (i) the Maturity Date, (ii) the conversion of all of the outstanding Debentures in accordance with Section 3.1 hereof or (iii) the date a Change of Control (as defined in the Purchase Agreement) occurs, 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 the Mandatory Conversion Notice 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 the 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 of Common Stock 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 Holder shall complete, execute and deliver to the Company the Assignment attached hereto as Attachment I. Upon receipt of a properly completed and executed Assignment in the form attached as Attachment I, 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; provided, however, that if, at the date of surrender the transfer books of the Common Stock shall be closed, the certificates for the Shares shall be issuable as of the date on which such books shall be opened and until such date the Company shall be under no duty to deliver any certificate for such Shares; provided, further, however, that such transfer books, unless otherwise required by law or by applicable rule of any national securities exchange, shall not be closed at any one time for a period longer than twenty (20) days.

3.4 Company to Provide Common Stock. The Company shall reserve out of its authorized but unissued shares of 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 endeavor to comply with all securities laws regulating the offer and delivery of the Shares upon conversion of the Debentures and will endeavor to 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 (a) the exercise of conversion rights hereunder by the Holder and (b) 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.

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 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, such 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, of which:

(A) the numerator shall be 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

(B) the denominator shall be 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 Conversion 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 and 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 March 10, 1998 (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 exchanged 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 III. 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. Except as expressly provided in the Purchase Agreement, no modification or waiver of any provision of this Debenture or any documents or instruments executed in connection herewith 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, 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 satisfactory to the Company of such loss, theft or destruction and an indemnity, if requested, also 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.

4.13 Amended and Restated Debenture. This Amended and Restated 5% Convertible Senior Secured Debenture dated as of December ___, 2002 issued by the Company in favor of the Payee is issued in accordance with that certain Amendment to Debenture and Warrant Purchase Agreement dated as December __, 2002 between the Company and the Purchasers listed on the signature page thereto (the

"Amendment") and amends and restates in their entirety, and is issued by the Company in replacement of and substitution for, each of those certain 5% Convertible Senior Secured Debenture instruments described on Schedule A, attached hereto, issued by the Company to the Payee (collectively, the "Original Debentures"). The Company and the Payee acknowledge and agree that upon the execution delivery of this Amended and Restated 5% Convertible Senior Secured Debenture due March 31, 2006, each of the Original Debentures shall be null and void and of no further legal force or effect.

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

ATTEST [SEAL]

HALSEY DRUG CO., INC.

_____

By:_____
Name: Michael Reicher
Title: Chief Executive Officer

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 Amended and Restated 5% Convertible Senior Secured Debenture due March 31, 2006 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

_____

EXHIBIT 10.11

SECOND AMENDMENT

TO

LOAN AGREEMENT

THIS SECOND AMENDMENT TO LOAN AGREEMENT, dated as of December 20, 2002 (the "Second Amendment"), is made and entered into by and between Halsey Drug Co., Inc., a New York corporation ("Borrower"), and Watson Pharmaceuticals, Inc., a Nevada corporation ("Lender").

RECITALS

WHEREAS, Borrower and Lender are parties to that certain Loan Agreement, dated as of March 29, 2000, as amended by a certain Amendment to Loan Agreement dated as of March 31, 2000 (as so amended, the "Loan Agreement"); and

WHEREAS, pursuant to a certain Debenture Purchase Agreement dated of even date herewith (the "2002 Purchase Agreement") executed by Borrower in favor of the several purchasers named therein (the "Purchasers"), Borrower will issue its 5% Convertible Senior Secured Debentures due March 31, 2006 in the aggregate principal amount of up to approximately $35,000,000 (the "2002 Debentures"); and

WHEREAS, as a condition to their investment in the 2002 Debentures, the Purchasers have required that Lender amend the Loan Agreement to extend the maturity date of the Loan Agreement from March 31, 2003 to March 31, 2006; and

WHEREAS, as a condition to its agreement to so extend the Maturity Date, the Lender has required that (i) the $3,901,331 principal amount of Borrower's payment obligations to Watson as of the date hereof under that certain Core Products Supply Agreement (as hereinafter defined) be added to the Borrower's secured Obligations under the Loan Agreement (such new obligations, the "New Obligations"), and (ii) that the interest rate on both the $17,500,000 principal amount currently outstanding pursuant to the Loan Agreement be increased to the interest rate on the New Obligations; and

NOW, THEREFORE, the parties hereto agree as follows.

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

"1. AMOUNT AND TERMS OF LOAN.

1.1 Term Loans. Subject to the terms herein, Lender has previously loaned to Borrower the aggregate principal amount of Seventeen Million Five Hundred Thousand Dollars ($17,500,000), and, as described in this Second Amendment, is adding to such principal amount the additional principal amount of Three Million Nine Hundred and One Thousand Three Hundred Thirty One Dollars ($3,901,331), representing excess payments made by Lender to Borrower pursuant to that certain Finished Goods Supply Agreement (Core Products), as defined and provided in Section 12.15 hereof (collectively, the "Loan"). Notwithstanding any prepayment of the Loan by Borrower, sums repaid hereunder may not be re-borrowed.

1.2 Promissory Notes. Borrower's obligation to pay the principal of, and interest on, the Loan shall be evidenced by two secured promissory notes (the "Notes"), duly executed and delivered by Borrower, the first such Note (the "Replacement Note") to be in the form attached as Exhibit A to this Second Amendment and representing the $17,500,000 principal balance originally loaned to Borrower pursuant to the Loan Agreement, and the second such Note (the "New Note") to be in the form attached as Exhibit B to this Second Amendment and representing the $3,901,331 principal balance being added to the Obligations as described in this Second Amendment. Upon execution and delivery of the Replacement Note, the Secured Promissory Note dated March 31, 2000 issued by Borrower to Lender in the principal amount of $17,500,000 shall be null and void and of no further legal force or effect."

2. The definition of "Obligations" set forth in Section 12.1 of the Loan Agreement is hereby amended in its entirety to read as follows:

" 'Obligations' shall mean all obligations, liabilities and indebtedness of every kind, nature and description of the Borrower and the Guarantors from time to time owing to the Lender or any Indemnitee under or in connection with the Loan Documents and the New

Note, whether direct or indirect, primary or secondary, joint or several, absolute or contingent, due or to become due, now existing or hereafter arising and however acquired and shall include, without limitation, all principal and interest on the Loan and, to the extent chargeable under any Loan Document or the New Note, all charges, expenses, fees and reasonable attorney's fees."

3. A new Section 12.15 is hereby added to the Loan Agreement as follows:

"12.15 Core Products Supply Agreement. Borrower and Lender are parties to a certain Finished Goods Supply Agreement (Core Products) dated March 29, 2000 (the "Original Core Products Supply Agreement"), as amended by that certain Amendment and Supplement No. 1 to Finished Goods Supply Agreement (Core Products) dated as of August 8, 2001 (the "Amendment to Core Products Supply Agreement," and together with the Original Core Products Supply Agreement as so amended, the "Core Products Supply Agreement"). In accordance with the terms of the Original Core Products Supply Agreement, Lender made certain minimum quarterly payments to Borrower resulting in payments to Borrower exceeding the purchase price of the quantities of products provided by Borrower to Lender under the Core Products Supply Agreement. As a result, Borrower and Lender executed the Amendment to Core Products Supply Agreement providing, among other items, (i) for the parties' agreement on the amount by which Lender's aggregate minimum quarterly payments made through and including the quarter ended December 31, 2000 exceeded the aggregate purchase price of the products supplied by Borrower during such period (the "Excess Payments"), and (ii) for Borrower's repayment obligation to Lender of the Excess Payments. Borrower and Lender acknowledge and agree that the outstanding balance of the Excess Payments as of December 20, 2002 equals Three Million Nine Hundred and One Thousand Three Hundred Thirty One Dollars ($3,901,331) (the "Core Products Amount"). In accordance with the terms of Article One hereof, the Core Products Amount has been added to the Obligations of Borrower hereunder. On the date of execution by the parties of the Second Amendment, Borrower shall execute and deliver to Lender the New Note, which shall evidence the New Obligations. Borrower and Lender covenant and agree to execute the Second Amendment to Finished Goods Supply Agreement (Core Products) in the form attached as Exhibit C to the Second Amendment in order to give effect to the terms of this Section 12.15."

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

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

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

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

"BORROWER"	"LENDER"
HALSEY DRUG CO., INC.	WATSON PHARMACEUTICALS, INC.
By:_____	By:_____
Name: Michael Reicher	Name: _____
Title: Chief Executive Officer	Title: _____

EXHIBIT A

Replacement Note

EXHIBIT B

New Note

EXHIBIT C

Second Amendment to Finished
Goods Supply Agreement (Core Products)

EXHIBIT 10.12

SECURED PROMISSORY NOTE

$17,500,000 December 20, 2002
Corona, California

1. Promise to Pay. For good and valuable consideration, the receipt of which is hereby acknowledged, HALSEY DRUG CO., INC., a New York corporation ("Maker"), promises to pay to WATSON PHARMACEUTICALS, INC., a Nevada corporation ("Watson"), or order (either, the "Holder"), on the Maturity Date (as defined below), unless sooner paid as provided in Section 4 hereof, the principal sum of Seventeen Million Five Hundred Thousand Dollars ($17,500,000), plus accrued unpaid interest thereon. The outstanding principal balance of this Note shall bear interest at a variable rate equal to the prime rate announced from time to time by Bank of America (the "Prime Rate") plus four and one-half percent (4.5%) per annum (the "Interest Rate") from the date such principal amount becomes outstanding to the date the principal sum is paid in full; provided, however, that if this Note is not paid in full on the Maturity Date, the unpaid balance of the Note shall bear interest therefrom and until paid at the Default Rate (as defined below). Payments of interest shall be due on the each March 31, June 30, September 30 and December 31 during the term of this Note commencing December 31, 2002. All payments under this Note shall be made to the order of the Holder at 311 Bonnie Circle, Corona, California, 92880, or such other address as Holder may designate in writing to Maker, in U.S. dollars, and shall be applied first to accrued unpaid interest, if any, and then to principal.

2. Maturity Date. The date that this Note shall mature, and the principal amount outstanding hereunder, plus accrued unpaid interest thereon and any charges pertaining thereto, shall become due and payable (the "Maturity Date") shall be March 31, 2006.

3. Loan and Security Agreements. Maker and Watson are party to that certain Loan Agreement, dated as of March 29, 2000, as amended by that certain Amendment to Loan Agreement dated as of March 31, 2000 and as further amended by that certain Second Amendment to Loan Agreement dated as of December 20, 2002 (as so amended, the "Loan Agreement"). The full and punctual payment and performance of this Note by Maker are secured and guaranteed by the Company General Security Agreement, the Company Collateral Assignments, the Stock Pledge Agreement, the Guaranties, the Guarantors Security Agreement, the Guarantor Collateral Assignments and the Mortgage, as those terms are defined in the Loan Agreement (the "Security Agreements"). The security interest granted to Holder under the Security Agreements extends to the proceeds of any sale or other transfer or disposition of such assets, whether by Maker, its affiliates, the Holder or any other person, that occurs prior to the payment in full of this Note. Copies of the Loan Agreement and the Security Agreements may be obtained from Maker without charge.

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

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

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

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

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

(c) there occurs any other event or circumstance that constitutes an "Event of Default" as defined in Section 9.1 of the Loan Agreement.

Upon the occurrence of any Event of Default, as defined hereinabove, at Holder's option, Holder may declare immediately due and payable, and on any such declaration there shall become immediately due and payable, the entire unpaid principal balance of this Note, together with all accrued and unpaid interest under this Note and any other sums owing at the time of such declaration pursuant to this Note, the Loan Agreement or the Security Agreements, and Holder shall be entitled to exercise all rights and remedies available to Holder under this Note, under the Loan Agreement and the Security Agreements and under applicable law, all of which rights and remedies shall be cumulative. Without limiting the generality of the foregoing, upon the occurrence of an Event of Default, the interest rate at which interest shall accrue on the principal sum and any other amounts that are due under this Note shall increase to the lower of (i) the Prime Rate plus six and one-half percent (6.5%) per annum or (ii) the maximum interest rate permitted under applicable law (the "Default Rate"), until all such amounts have been paid in full.

7. No Waiver by Holder. Any delay or omission on the part of Holder to exercise any of Holder's rights or remedies hereunder, under the Loan Agreement or the Security Agreements or under applicable law, including, without limitation, the right to accelerate amounts owing under this Note, shall not be deemed a waiver of that right or remedy or of any other right or remedy of Holder in respect thereof. The acceptance by Holder of any payment pursuant to the terms of this Note which is less than payment in full of all

amounts due and payable at the time of such payment shall not constitute a waiver of the right to exercise any of the Holder's rights or remedies under this Note, the Loan Agreement, the Security Agreements or under applicable law at that time or at any subsequent time or nullify any prior exercise of any such rights or remedies without the express written consent of Holder, except as and to the extent provided to the contrary by applicable law.

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

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

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

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

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

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

14. Replacement Note. This Note is issued in accordance with that certain Second Amendment to Loan Agreement dated as of December 20, 2002, between Maker and Watson (the "Second Amendment"), and is issued by Maker in replacement of and substitution for, and represents the agreement of Maker and Watson to increase the interest rate on, and extend the maturity date of, that certain Secured Promissory Note issued by Maker to Watson in the principal amount of $17,500,000 dated March 31, 2000 (the "Original Note"). Upon execution and delivery of this Secured Promissory Note to Watson, the Original Note shall be null and void and of no further legal force or effect.

[SIGNATURE PAGE TO FOLLOW]

"MAKER"

HALSEY DRUG CO., INC.

_____
By: Michael Reicher
Its: Chief Executive Officer

EXHIBIT 10.13

SECURED PROMISSORY NOTE

$3,901,331 December 20, 2002
Corona, California

1. Promise to Pay. For good and valuable consideration, the receipt of which is hereby acknowledged, HALSEY DRUG CO., INC., a New York corporation ("Maker"), promises to pay to WATSON PHARMACEUTICALS, INC., a Nevada corporation ("Watson"), or order (either, the "Holder"), on the Maturity Date (as defined below), unless sooner paid as provided in Section 4 hereof, the principal sum of Three Million Nine Hundred and One Thousand Three Hundred Thirty One Dollars ($3,901,331), plus accrued unpaid interest thereon. The outstanding principal balance of this Note shall bear interest at a variable rate equal to the prime rate announced from time to time by Bank of America (the "Prime Rate") plus four and one-half percent (4.5%) per annum (the "Interest Rate") from the date such principal amount becomes outstanding to the date the principal sum is paid in full; provided, however, that if this Note is not paid in full on the Maturity Date, the unpaid balance of the Note shall bear interest therefrom and until paid at the Default Rate (as defined below). Payments of interest shall be due on the each March 31, June 30, September 30 and December 31 during the term of this Note commencing December 31, 2002. All payments under this Note shall be made to the order of the Holder at 311 Bonnie Circle, Corona, California, 92880, or such other address as Holder may designate in writing to Maker, in U.S. dollars, and shall be applied first to accrued unpaid interest, if any, and then to principal.

2. Maturity Date. The date that this Note shall mature, and the principal amount outstanding hereunder, plus accrued unpaid interest thereon and any charges pertaining thereto, shall become due and payable (the "Maturity Date") shall be March 31, 2006.

3. Loan and Security Agreements. Maker and Watson are party to that certain Loan Agreement, dated as of March 29, 2000, as amended by that certain Amendment to Loan Agreement dated as of March 31, 2000 and as further amended by that certain Second Amendment to Loan Agreement dated as of December 20, 2002 (as so amended, the "Loan Agreement"). This Note is being issued pursuant to said Second Amendment, and it is the intention of the Maker and Watson that the full and punctual payment and performance of this Note by Maker be secured and guaranteed by the Company General Security Agreement, the Company Collateral Assignments, the Stock Pledge Agreement, the Guaranties, the Guarantors Security Agreement, the Guarantor Collateral Assignments and the Mortgage, as those terms are defined in the Loan Agreement (the "Security Agreements"). The security interest granted to Holder under the Security Agreements extends to the proceeds of any sale or other transfer or disposition of such assets, whether by Maker, its affiliates, the Holder or any other person, that occurs prior to the payment in full of this Note. Copies of the Loan Agreement and the Security Agreements may be obtained from Maker without charge.

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

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

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

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

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

(c) there occurs any other event or circumstance that constitutes an "Event of Default" as defined in Section 9.1 of the Loan Agreement.

Upon the occurrence of any Event of Default, as defined hereinabove, at Holder's option, Holder may declare immediately due and payable, and on any such declaration there shall become immediately due and payable, the entire unpaid principal balance of this Note, together with all accrued and unpaid interest under this Note and any other sums owing at the time of such declaration pursuant to this Note, the Loan Agreement or the Security Agreements, and Holder shall be entitled to exercise all rights and remedies available to Holder under this Note, under the Loan Agreement and the Security Agreements and under applicable law, all of which rights and remedies shall be cumulative. Without limiting the generality of the foregoing, upon the occurrence of an Event of Default, the interest rate at which interest shall accrue on the principal sum and any other amounts that are due under this Note shall increase to the lower of (i) the Prime Rate plus six and one-half percent (6.5%) per annum or (ii) the maximum interest rate permitted under applicable law (the "Default Rate"), until all such amounts have been paid in full.

7. No Waiver by Holder. Any delay or omission on the part of Holder to exercise any of Holder's rights or remedies hereunder, under the Loan Agreement or the Security Agreements or under applicable law, including, without limitation, the right to accelerate amounts owing under this Note, shall not be deemed a waiver of that right or remedy or of any other right or remedy of Holder in respect thereof. The acceptance by Holder of any payment pursuant to the terms of this Note which is less than payment in full of all

amounts due and payable at the time of such payment shall not constitute a waiver of the right to exercise any of the Holder's rights or remedies under this Note, the Loan Agreement, the Security Agreements or under applicable law at that time or at any subsequent time or nullify any prior exercise of any such rights or remedies without the express written consent of Holder, except as and to the extent provided to the contrary by applicable law.

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

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

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

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

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

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

14. Relation Back of Note. This Note is issued in accordance with that certain Second Amendment to Loan Agreement dated as of December 20, 2002, between Maker and Watson (the "Second Amendment"). Maker and Watson acknowledge and agree that the principal amount of this Secured Promissory Note represents the full amount of the Core Products Amount of $3,901,331 (as defined and provided in the Second Amendment), which was heretofore unsecured, and expressly intend that Maker's obligations pursuant to this Secured Promissory Note be added to the obligations of Maker secured by the Security Agreements.

"MAKER"

HALSEY DRUG CO., INC.

_____
By: Michael Reicher
Its: Chief Executive Officer

EXHIBIT 10.14

SECOND AMENDMENT
TO FINISHED GOODS SUPPLY AGREEMENT
(CORE PRODUCTS)

This Second Amendment (this "Second Amendment") to the Finished Goods Supply Agreement (Core Products) dated the 29th day of March, 2000, between Watson Pharmaceuticals, Inc., a Nevada corporation ("Watson"), and Halsey Drug Co., Inc., a New York corporation ("Halsey") (the "Original Core Products Agreement"), as amended pursuant to that certain Amendment and Supplement No. 1 to Finished Goods Supply Agreement (Core Products) dated as of August 8, 2001, (the "First Amendment" and collectively with the Original Core Products Agreement, the "Core Products Agreement"), is made as of this 20th day of December, 2002.

RECITALS

A. Watson and Halsey entered into the Original Core Products Agreement pursuant to which Halsey (or its appropriate Affiliates) agreed to supply and Watson (or its appropriate Affiliates) agreed to purchase the Commercial Products.

B. Pursuant to Section 2.6 of the Original Core Products Agreement Watson made certain minimum quarterly payments to Halsey for Commercial Products (the "Minimum Payments").

C. The Minimum Payments made by Watson exceeded the aggregate purchase price of the Commercial Products supplied by Halsey, resulting in a credit to Watson for excess Minimum Payments of $4,402,682.60 through and including the quarter ended December 31, 2000 (the "Core Products Credit Amount").

D. Watson and Halsey entered into the First Amendment to, among other things, (i) agree upon the Core Products Credit Amount, (ii) reduce Watson's minimum quarterly payments to Halsey and (iii) provide for the application of the Core Products Credit Amount against future purchases of Commercial Products from Halsey, and for the repayment by Halsey of the remaining balance of the Core Products Credit Amount in equal monthly installments in October and November 2002.

E. Watson and Halsey are parties to a certain Loan Agreement dated as of March 29, 2000, as amended by that certain Amendment to Loan Agreement dated as of March 31, 2000 (as so amended, the "Loan Agreement") pursuant to which Watson has made a term loan to Halsey in the principal amount of $17,500,000 (the "Loan").

F. Watson and Halsey propose to amend the Loan Agreement pursuant to a certain Second Amendment to Loan Agreement dated as of even date providing, among other items, for the inclusion of the current balance of the Core Products Credit Amount

as of the date hereof of $3,901,331 (the "Core Products Rollover Amount") in the principal amount of the Loan.

G. Watson and Halsey desire to amend the Core Products Agreement to reflect the inclusion of the Core Products Rollover Agreement in the Loan.

In consideration of the foregoing premises, and the mutual covenants and obligations set forth herein, Halsey and Watson hereby agree as follows:

1. Definitions. All capitalized terms used herein and not otherwise defined shall have the meaning set forth in the Core Products Agreement.

2. Section 2.7 of the Agreement is hereby deleted in its entirety and the following inserted in its place:

> "2.7 Credits. Halsey acknowledges that as of December 20, 2002, Watson has paid to Halsey an aggregate of $3,901,331 in excess of the aggregate purchase price of Commercial Products supplied by Halsey to Watson under the Agreement (the "Core Products Rollover Amount"). Watson and Halsey acknowledge and agree that effective as of December 20, 2002 (i) the Core Products Rollover Amount shall be included in the Loan (as defined in the Second Amendment hereto) and subject to the terms and provisions of the principal amount of the Loan Agreement (as defined in the Second Amendment hereto), and (ii) except for its obligations under the Loan, Halsey shall have no further liability to Watson for the Core Products Rollover Amount."

3. Surviving Provisions. Watson and Halsey agree that except as expressly modified herein all provisions of the Core Products Agreement shall remain in full force and effect.

IN WITNESS WHEREOF, the parties have caused this Second Amendment to be executed by their respective duly authorized officers as of the date first above written.

WATSON PHARMACEUTICALS, INC.

By:_____
Name:_____
Title:_____

HALSEY DRUG CO., INC.

By:_____
Name: Michael Reicher
Title: Chief Executive Officer

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 LAWS 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, WATSON PHARMACEUTICALS, INC., or its 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) 10,700,665 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 $.34 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 December 31, 2009.

This Warrant is subject to the following terms and conditions:

1. Exercise of Warrant.

(a) 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), 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 (i) 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, (ii) 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 (iii) 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 (iv) 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 of the Company. 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)(iv) 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.

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 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 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.

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) Until such time as the Company completes a Subsequent Material Offering (as defined in Section 3(k) hereof), if 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"), including in connection with a Subsequent Material Offering, other than:

(i) shares issued in a transaction described in subsection (d) of this Section 3; or

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

for a consideration per share which is less than the Warrant Price in effect immediately prior to such issuance or sale (the "Applicable Warrant Price"), then the Applicable Warrant Price in effect immediately prior to such issuance or sale shall, and thereafter, except as otherwise provided in Subsection 3(c) hereof, upon each issuance or sale for a consideration per share which is less than the Applicable Warrant Price, the Applicable Warrant Price shall, simultaneously with such issuance or sale, be adjusted, so that such Applicable Warrant Price shall equal (A) the price per share received by the Company, in the case of the issuance of Common Stock by the Company, or (B) the exercise or conversion price of the Convertible Securities issued by the Company, as applicable.

(c) If at any time following the Company's completion of a Subsequent Material Offering the Company shall grant or issue any shares of Common Stock, or grant or issue any Convertible Securities, other than:

(i) shares issued in a transaction described in subsection (d) of this Section 3; or

(ii) shares issued, subdivided or combined in transactions described in Section 3(a) 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(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 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 the Applicable Warrant Price shall equal a price determined by multiplying the Applicable Warrant Price by a fraction, of which:

(A) the numerator of which shall be 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 Section 3(e) for the issuance or sale of such additional Common Stock or Convertible Securities deemed to be an issuance of Common Stock as provided in Section 3(f), 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(c)) at the Fair Market Value of the Common Stock; and

(B) the denominator of which shall be the total number of shares of Common Stock outstanding (or deemed to be outstanding as provided in subsection 3(f) 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 solely pursuant to this subsection 3(c), the Warrantholder shall thereafter be entitled to acquire upon exercise under Section 1, at the Applicable Warrant Price, 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.

(d) 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 or Convertible Securities issued in satisfaction of interest payments on all of the Company's 5% convertible senior secured debentures due March 31, 2006, including (i) the 5% convertible senior secured debentures issued pursuant to the Debenture and Warrant Purchase Agreement dated as of March 10, 1998 between the Company, Galen Partners III, L.P. and the other signatories thereto, the Debenture and Warrant Purchase Agreement dated as of May 26, 1999 between the Company, Oracle Strategic Partners, L.P. and the other signatories thereto, and the Debenture Purchase Agreement dated December 20, 2002 between the Company, Care Capital LLC, Essex Woodlands Health Ventures Fund V and the other signatories thereto, and (ii) the issuance of Common Stock or Convertible Securities issued in satisfaction of interest payments on debentures instruments issued by the Company in satisfaction of interest payments on the Company's 5% convertible senior secured debentures due March 31, 2006; or

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

(v) the issuance of the Company's 5% convertible senior secured debentures due March 31, 2006 issued pursuant to that certain Debenture Purchase Agreement dated December 20, 2002 between the Company, Care Capital, LLC, Essex Woodlands Health Ventures Fund V and the other purchasers listed on the signature page thereto; or

(vi) the issuance of 5,970,083 shares of the Company's Common Stock pursuant to that certain Warrant Recapitalization Agreement dated December 20, 2002 between the Company, Oracle Strategic Partners, L.P. and the other parties listed on the signature page thereto.

(e) For the purpose of Sections 3(b), 3(c) and 3(d), 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 market 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 exchanged 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.

(f) For purposes of the adjustment provided for in Sections 3(b) and 3(c) 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.

(g) 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 (i) 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 (ii) had all subsequent adjustments been made on only the basis of the Warrant Price as readjusted under this Section 3(g) for all transactions (which would have affected such adjusted Warrant Price) made after the issuance or sale of such Convertible Securities.

(h) 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

Section 3(h) 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.

(i) 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 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 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.

(j) 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 Section 3(j) applies, Section 3(a) does not apply.

(k) For purposes hereof, "Subsequent Material Offering" shall mean the grant or issuance of shares of Common Stock, or the grant or issuance of Convertible Securities, during any six (6) month period for an aggregate gross consideration (determined in accordance with Section 3(e) hereof) of at least ten million dollars ($10,000,000) for a consideration per share that is in excess of the then Applicable Exercise Price.

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.

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 December 20, 2002

HALSEY DRUG CO., INC.

BY:_____
Name: Michael Reicher
Title: Chief Executive Officer

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 10.16

REGISTRATION RIGHTS AGREEMENT

THIS REGISTRATION RIGHTS AGREEMENT (this "Agreement") dated as of December 20, 2002, by and between HALSEY DRUG CO., INC., a New York corporation (the "Company") and the investors listed on Schedule 1 attached hereto (each an "Investor"; collectively, the "Investors").

WHEREAS, the Company and certain purchasers are parties to that certain Debenture and Warrant Purchase Agreement dated March 10, 1998 (as such agreement may be supplemented, amended, or otherwise modified from time to time, the "1998 Purchase Agreement"), whereby the Company issued to such parties the Company's 5% convertible secured debentures due March 15, 2003 (as such debentures may be supplemented, amended, or otherwise modified from time to time, the "1998 Debentures"; each such holder of 1998 Debentures, or any permitted successor, assign or transferee thereof, a "1998 Holder") and warrants to purchase Common Stock (the "1998 Warrants");

WHEREAS, in connection with the 1998 Purchase Agreement, the Company granted to the 1998 Holders registration rights as set forth in Article XI of the 1998 Purchase Agreement;

WHEREAS, the Company and certain purchasers are parties to that certain Debenture and Warrant Purchase Agreement dated May 26, 1999 (as such agreement may be supplemented, amended, or otherwise modified from time to time, the "1999 Purchase Agreement"), whereby the Company issued to such parties the Company's 5% convertible secured debentures due March 15, 2003 (as such debentures may be supplemented, amended, or otherwise modified from time to time, the "1999 Debentures"; each such holder of 1999 Debentures, or any permitted successor, assign or transferee thereof, a "1999 Holder") and warrants to purchase Common Stock (the "1999 Warrants");

WHEREAS, in connection with the 1999 Purchase Agreement, the Company granted to the 1999 Holders registration rights as set forth in Article XI of the 1999 Purchase Agreement;

WHEREAS, in connection with the Bridge Loan Agreements, Galen Partners III, L.P., Galen Partners International III, L.P. and Galen Employee Fund III, L.P. (collectively, "Galen") holds warrants to purchase an aggregate of 5,385,229 shares of the Company's common stock, $.01 par value per share (the "Common Stock") as more particularly described on Schedule 2 hereof (the "Bridge Loan Warrants");

WHEREAS, the Company and Watson Pharmaceuticals, Inc. ("Watson") are parties to that certain Loan Agreement, dated as of March 29, 2000, as amended by a certain Amendment to Loan Agreement dated as of March 31, 2000 (as so amended, the "Loan Agreement");

WHEREAS, in consideration of further amending the Loan Agreement to, among other things, extend the maturity date of the loan by execution of a Second Amendment to the Loan Agreement dated as of December __, 2002, simultaneously with the execution of this Agreement, the Company will issue to Watson a warrant (the "Watson Warrant") to purchase 10,700,665 shares of the Common Stock;

WHEREAS, in connection with the 2002 Purchase Agreement, all of the holders (except Galen) (the "Recap Shareholders") of the 1998 Warrants and the 1999 Warrants have entered into an agreement (the "Recapitalization Agreement"), dated the date hereof, to recapitalize their interests in the Company by, inter alia, exchanging their respective warrants for shares of Common Stock (the "Recap Shares");

WHEREAS, the Company and certain purchasers are parties to that certain Debenture Purchase Agreement, dated the date hereof (as such agreement may be supplemented, amended, or otherwise modified from time to time, the "2002 Purchase Agreement"), whereby the Company issued to such parties the Company's 5% convertible senior secured debentures due March 31, 2006 (as such debentures may be supplemented, amended, or otherwise modified from time to time, the "2002 Debentures"; each such holder of 2002 Debentures, or any permitted successor, assign or transferee thereof, a "2002 Holder");

WHEREAS, in connection with the 2002 Purchase Agreement, the Company has agreed to grant to the 2002 Holders registration rights as set forth in this Agreement;

WHEREAS, the 1998 Holders desire to terminate the registration rights provisions of the 1998 Purchase Agreement, the 1999 Holders desire to terminate the registration rights provisions of the 1999 Purchase Agreement, the holders of the 1998 Warrants desire to terminate the registration rights applicable to the 1998 Warrants, the holders of the 1999 Warrants desire to terminate the registration rights applicable to the 1999 Warrants, and Galen desires to terminate the registration rights applicable to the Bridge Loan Warrants and such parties desire to enter into this Agreement in lieu therefor to provide for generally applicable registration rights for all such parties, to the extent applicable, and to Watson and the 2002 Holders;

WHEREAS, the Company desires to grant and Watson, the 1998 Holders, the 1999 Holders, the 2002 Holders, the Recap Shareholders and Galen desire to obtain, certain registration rights in connection with the Recap Shares, the Watson Warrant, the 1998 Debentures, the 1999 Debentures, the 1998 Warrants held by Galen, the 1999 Warrants held by Galen, the Bridge Loan Warrants and the 2002 Debentures (collectively, the "Securities"); and

WHEREAS, unless otherwise provided in this Agreement, capitalized terms used herein shall have the meanings set forth in Section 14 hereof.

NOW, THEREFORE, in consideration of the foregoing and the mutual covenants and promises contained herein, the parties agree as follows:

1. Demand Registrations.

(A) Requests for Registration. The Holders may request registration under the Securities Act of all or any part of their Registrable Securities as provided for below in Section 1(b). Within ten days after receipt of any such request, the Company will give written notice of such requested registration to all other Holders of Registrable Securities. The Company will include in such registration all Registrable Securities with respect to which it has received written requests for inclusion therein within 30 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 1 is referred to herein as a "Demand Registration".

(B) Number of Registrations. The Holders of Registrable Securities will be entitled to request the following number and types of registrations: (i) Galen shall be entitled to request two Demand Registrations on Form S-1 (or any successor to such form), (ii) Watson shall be entitled to request two Demand Registrations on Form S-1 (or any successor to such form), (iii) the Holders of at least 20% of the Registrable Securities then outstanding shall be entitled to request one Demand Registration on Form S-1 (or any successor to such form), provided that all Demand Registrations requested pursuant to subsections (i) and (ii) above shall be deemed to have occurred prior to the Demand Registration pursuant to this subsection (iii), and (iv) the Holders of Registrable Securities will be entitled to unlimited Demand Registrations on Form S-3 (or any successor to such form), for which the Company will pay all Registration Expenses. A registration will not count as a Demand Registration (x) until it has become effective, (y) the Holders have sold, in the aggregate, no less than 50% of the shares of Registrable Securities requested to be registered in the Demand Registration and (z) if the offering of the Registrable Securities pursuant to such registration is interfered with for any reason by any stop order, injunction or other order or requirement of the Commission (other than any stop order, injunction or other requirement of the Commission prompted by acts or omissions of Holders of Registrable Securities); provided, however, that except as otherwise provided herein 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 with respect to 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. If the amount of such Registrable Securities does not exceed the maximum number which can be sold in such offering, the Company may include such number of securities which are not Registrable Securities in the Demand Registration which will not, together with the Holder's Registrable Securities, exceed the maximum number which can be sold in the Offering; provided, however, the Company will not include in any Demand Registration any securities which are not Registrable Securities without the written consent of the Holders of sixty and two-thirds percent (66 2/3%) of the Registrable Securities participating in such registration. A registration shall not count as a Demand Registration if less than fifty percent (50%) 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 1(c).

(D) Restrictions on Demand Registrations. The Company will not be obligated to effect any Demand Registration within six months after the effective date of a previous registration in which the Holders of Registrable Securities were given piggyback rights pursuant to Section 2 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").

2. 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 the Holders of Registrable Securities. The Company will include in such registration all Registrable Securities with respect to which the Company has received written requests for inclusion therein within 30 days after the receipt of the Company's notice, subject to any other priority cutback provisions below.

(B) Piggyback Expenses. The Registration Expenses of the Holders of Registrable Securities in such Piggyback Registration 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, pro rata in accordance with the amounts of Registrable Securities requested to be so included by each Requesting Stockholder, 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, pro rata in accordance with the amounts of Registrable Securities requested to be so included by each Requesting Stockholder, 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 1 or pursuant to this Section 2, 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 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.

3. Holdback Agreements.

(A) Holders of Registrable Securities. The Investors and each other Holder of Registrable Securities who is or becomes 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 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. 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 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; provided, however, that the provisions of this Section 3(b) shall continue to apply with respect to a registration until the provisions of Section 3(a) no longer apply with respect to such registration.

(C) Registration Procedures. Whenever the Holders of Registrable Securities have requested that any Registrable Securities be registered pursuant to Section 1 or 2 of this Agreement, the Company shall use its 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 shall as expeditiously as possible:

(i) 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 successor rule under the Securities Act), 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 (A) Galen, in the event of a Demand Registration requested pursuant to Section 1(b)(i), (B) Watson, in the event of a Demand Registration requested pursuant to Section 1(b)(ii), or (C) the Holders of sixty and two-thirds percent (66 2/3%) of the Registrable Securities included in such registration, in the event of any other registration, copies of all such documents proposed to be filed, which documents will be subject to the review of such counsel);

(ii) 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 4(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;

(iii) 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;

(iv) use its best efforts to register or qualify, if applicable, 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 (A) qualify generally to do business in any jurisdiction where it would not otherwise be required to qualify but for this subsection, (B) subject itself to taxation in any such jurisdiction, or (C) consent to general service of process in any such jurisdiction);

(v) within one business day of its occurrence, 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;

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

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

(viii) 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;

(ix) 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 Holders of sixty-six and two-thirds percent (66-2/3%) of the Registrable Securities included in such registration, and keep such registration statement effective until the Holders of a sixty-six and two-thirds percent (66-2/3%) of Registrable Securities included in such registration have completed the sale and distribution of the Registrable Securities;

(x) if such registration is an underwritten registration, cause the Company's officers, directors and holders of in excess of one percent of the Company's outstanding Common to execute lock-up agreements, containing customary terms and provisions, required by an underwriter in any such registered offering restricting such parties from selling shares of the Company's Common Stock for a period of up to 180 days; and

(xi) furnish, at the request of any Holder requesting registration of Registrable Securities pursuant to Section 1 or 2, if the method of distribution is by means of an underwriting, on the date that the shares of Registrable Securities are delivered to the underwriters for sale pursuant to such registration, or if such Registrable Securities are not being sold through underwriters, on the date that the registration statement with

respect to such shares of Registrable Securities becomes effective, (A) a signed opinion, dated such date, of the independent legal counsel representing the Company for the purpose of such registration, addressed to the underwriters, if any, and if such Registrable Securities are not being sold through underwriters, then to the Holders making such request, as to such matters as such underwriters or the Holders holding a majority of the Registrable Securities included in such registration, as the case may be, may reasonably request; and (B) letters dated such date and the date the offering is priced from the independent certified public accountants of the Company, addressed to the underwriters, if any, and if such Registrable Securities are not being sold through underwriters, then to the Holders making such request (x) stating that they are independent certified public accountants within the meaning of the Act and that, in the opinion of such accountants, the financial statements and other financial data of the Company included in the Registration Statement or the prospectus, or any amendment or supplement thereto, comply as to form in all material respects with the applicable accounting requirements of the Act and (y) covering such other financial matters (including information as to the period ending not more than five business days prior to the date of such letters) with respect to the registration in respect of which such letter is being given as such underwriters or the Holders holding a majority of the Registrable Securities included in such registration, as the case may be, may reasonably request and as would be customary in such a transaction.

4. Registration Expenses. All Registration Expenses incurred in connection with a registration, qualification or compliance pursuant to this Agreement shall be borne by the Company, and all Selling Expenses shall be borne by the Holders, the Requesting Stockholders and any other holders 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 a majority of Registrable Securities (other than as a result of any failure of the Company to comply with the terms of this Agreement, or the disclosure of any adverse development relating to the Company after the initial request for registration by any Holder), 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 1.

5. Indemnification.

(A) The Company will indemnify each Holder, each Holder's officers, directors, employees, agents, members and partners, and each Person controlling, controlled by or under common control with such Holder, with respect to which registration, qualification or compliance of such Holder's securities has been effected pursuant to this Agreement, and each underwriter, if any, and each Person who controls any underwriter, against all claims, losses, damages and liabilities (or actions in respect thereof), joint or several, 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, members and partners, and each Person controlling each 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 to a Holder 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 severally not jointly, 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, Requesting Stockholder or any other holder of securities included in the offering and each of their respective officers, directors, employees, agents, members and partners, and each Person controlling such other Holder, Requesting Stockholder and any other holders of securities included in the offering, against all claims, losses, damages and liabilities (or actions in respect thereof), joint or several, 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, members, 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 such Holder and Requesting Stockholder hereunder shall be limited to an amount equal to the net proceeds (after deduction of underwriting discounts and selling commissions, if any) received by each such Holder or Requesting Stockholder of securities sold as contemplated herein.

(C) Each party entitled to indemnification under this Section 5 (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 Agreement 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.

6. Restrictive Legend. Each certificate representing (a) the Securities or (b) any Shares or other securities issued in respect thereof, upon any stock split, stock dividend, recapitalization, merger, consolidation or similar event shall be stamped or otherwise imprinted with a legend in the following form (in addition to any legend required under applicable state securities laws and any other applicable agreement(s)):

> "THIS WARRANT/DEBENTURE [AND THE COMMON STOCK ISSUABLE UPON COVERSION HEREOF] HAVE NOT BEEN REGISTERED UNDER THE SECURITIES ACT OF 1933, AS AMENDED (THE "ACT"), 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 LAWS OR (2) THE COMPANY RECEIVES AN OPINION OF COUNSEL TO THE COMPANY OR OTHER COUNSEL TO THE HOLDER OF SUCH [WARRANT/DEBENTURE AND/OR COMMON STOCK] REASONABLY SATISFACTORY TO THE COMPANY THAT SUCH [WARRANT/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."

7. Information by the Holders and Requesting Stockholders. 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 Agreement.

8. 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 that are more favorable to such holder or prospective holder than the rights granted under this Agreement.

9. 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 ("Rule 144"), 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 Exchange Act at any time after it has become subject to such reporting requirements; and

(c) so long as the Holders own any Restricted Securities, furnish to the Holders forthwith upon request a written statement by the Company as to its compliance with the reporting requirements of Rule 144 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 any Holder may reasonably request in availing itself of any rule or regulation of the Commission allowing any Holder to sell any such securities without registration.

10. Participation in Underwritten Registrations. Subject to the right of any Holder or Holders to withdraw any request for registration, no Person may participate in any underwritten registration hereunder unless such Person (a) 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 (b) completes and executes all reasonable and customary questionnaires, powers of attorney, indemnities, underwriting agreements and other documents required under the terms of such underwriting arrangements.

11. Selection of Underwriters. If any Demand Registration is an underwritten offering, (a) Galen, in the event of a Demand Registration requested pursuant to Section 1(b)(i), (b) Watson, in the event of a Demand Registration requested pursuant to Section 1(b)(ii), and (c) the Holders of sixty and two-thirds percent (66 2/3%) of the Registrable Securities included in such registration, in the event of any other registration shall have the right to select the

investment banking firm to be lead manager of 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 banking firm to be lead manager of the offering, subject to the approval of the Holders of sixty and two-thirds percent (66 2/3%) of the Registrable Securities included in such registration (which approval will not be unreasonably withheld).

12. Termination of Registration Rights. The rights of Holders to request a Demand Registration or participate in a Piggyback Registration shall expire on March 31, 2008.

13. Termination of Other Registration Rights Agreements.

(a) The 1998 Holders hereby agree and acknowledge that in consideration for the registration rights granted hereunder that Article XI (or any successor or equivalent article or provision) of the 1998 Purchase Agreement and any other agreement, instrument or understanding that grants or purports to grant registration rights to such parties are hereby terminated and of no further force or effect.

(b) The holders of the 1998 Warrants hereby agree and acknowledge that in consideration for the registration rights granted hereunder that Article XI (or any successor or equivalent article or provision) of the 1998 Purchase Agreement and any other agreement, instrument or understanding that grants or purports to grant registration rights to such parties are hereby terminated and of no further force or effect.

(c) The 1999 Holders hereby agree and acknowledge that in consideration for the registration rights granted hereunder that Article XI (or any successor or equivalent article or provision) of the 1999 Purchase Agreement and any other agreement, instrument or understanding that grants or purports to grant registration rights to such parties are hereby terminated and of no further force or effect.

(d) The holders of the 1999 Warrants hereby agree and acknowledge that in consideration for the registration rights granted hereunder that Article XI (or any successor or equivalent article or provision) of the 1999 Purchase Agreement and any other agreement, instrument or understanding that grants or purports to grant registration rights to such parties are hereby terminated and of no further force or effect.

(e) Galen hereby agrees and acknowledges that in consideration for the registration rights granted hereunder that any provision or Section in the Bridge Loan Agreements, the Bridge Loan Warrants and any other agreement, instrument or understanding that grants or purports to grant registration rights to Galen are hereby terminated and of no further force or effect.

14. Definitions. As used herein, the following terms have the following meanings:

"Act" means the Securities Act of 1933, as amended.

"Agreement" means this Registration Rights Agreement.

"Bridge Loan Agreements" means any and all of the separate Bridge Loan Agreements between the Company, Galen Partners III, L.P. and the other parties listed on the signature pages thereto entered into between such parties commencing as of August 12, 1998 through and including December __, 2002 pursuant to which the Bridge Loan Warrants were issued, including, without limitation, that certain Bridge Loan Agreement dated as of August 15, 2001 among the Company, Galen Partners III, L.P., Galen Partners International III L.P., Galen Employee Fund III, L.P., those individuals listed on the signature page thereto, and Galen Partners III, L.P., as agent for the lenders, as amended by the First Amendment to Bridge Loan Agreement dated as of January 8, 2002, the Second Amendment to Bridge Loan Agreement dated as of April 5, 2002, and the Third Amendment to Bridge Loan Agreement dated as of May 8, 2002, as such may be supplemented, amended or otherwise modified from time to time.

"Common Stock" has the meaning set forth in the recitals.

"Commission" means the Securities and Exchange Commission.

"Company" has the meaning set forth in the preamble.

"Demand Registration" has the meaning set forth in Section 1(a) of this Agreement.

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

"Holders" means the Investors or any Person to whom an Investor or transferee(s) of an Investor has assigned, transferred or otherwise conveyed the Securities or the Shares.

"Indemnified Party" has the meaning set forth in Section 5 hereof.

"Indemnifying Party" has the meaning set forth in Section 5 hereof.

"Investors" has the meaning set forth in the preamble.

"Loan Agreement" has the meaning set forth in the recitals.

"1998 Debentures" has the meaning set forth in the recitals.

"1998 Holder" has the meaning set forth in the recitals.

"1998 Purchase Agreement" has the meaning set forth in the recitals.

"1998 Warrants" has the meaning set forth in the recitals.

"1999 Debentures" has the meaning set forth in the recitals.

"1999 Holder" has the meaning set forth in the recitals.

"1999 Purchase Agreement" has the meaning set forth in the recitals.

"1999 Warrants" has the meaning set forth in the recitals.

"Person" means any individual, corporation, limited liability company, partnership, association, trust or any other entity or organization, including a government or political subdivision or an agency or instrumentality thereof.

"Piggyback Registration" has the meaning set forth in Section 2 of this Agreement.

"Registrable Securities" means any Shares issued or issuable upon the exercise or conversion of the Securities (including any Securities that may be issued as interest with respect to any Security) or in respect of the Shares issued or issuable upon the exercise or conversion of any Securities upon any stock split, stock dividend, recapitalization or similar event.

"Registration Expenses" means all expenses incurred by the Company in compliance with Sections 1 and 2 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, as such counsel is selected in accordance with Section 4(a), and the expense of any special audits incident to or required by any such registration, exclusive of the Selling Expenses.

"Restricted Securities" means the securities of the Company required to bear or bearing the legend set forth in Section 6 of this Agreement.

"Requesting Stockholders" means holders of securities of the Company entitled to have securities included in any registration pursuant to Section 2 and who shall request such inclusion.

"Rule 144" has the meaning set forth in Section 9 of this Agreement.

"Securities" has the meaning set forth in the recitals.

"Securities Act" means the Securities Act of 1933, as amended.

"Selling Expenses" means 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.

"Shares" means the shares of Common Stock which may be issued upon the exercise of all or a portion of the Securities. The term Shares does not include any other shares of Common Stock or other capital stock of the Company.

"Shelf Registration" has the meaning set forth in Section 1 of this Agreement.

"2002 Debentures" has the meaning set forth in the recitals.

"2002 Holder" has the meaning set forth in the recitals.

"2002 Purchase Agreement" has the meaning set forth in the recitals.

"Watson Warrant" has the meaning set forth in the recitals.

15. Remedies. Any Person having rights under any provision of this Agreement shall be entitled to enforce such rights specifically to recover damages caused by reason of any breach of any provision of this Agreement and to exercise all other rights granted by law. The parties hereto agree and acknowledge that money damages may not be an adequate remedy for any breach of the provisions of this Agreement and that any party may in its sole discretion apply to any court of law or equity of competent jurisdiction (without posting any bond or other security) for specific performance and for other injunctive relief in order to enforce or prevent violation of the provisions of this Agreement.

16. Amendments and Waivers. The provisions of this Agreement may be amended or waived only upon the prior written consent of the Company and the Holders of sixty and two-thirds percent (66 2/3%) of the Registrable Securities, provided that the prior written consent of all of the Holders will be required to amend Section 1 and 2 hereof.

17 Delays or Omissions. No delay or omission to exercise any right, power or remedy accruing to any Investor or Holder upon any breach or default of the Company under this Agreement shall impair any such right, power or remedy of such Holder or Investor 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 Investor or 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.

18. Successors and Assigns. All covenants and agreements in this Agreement by or on behalf of any of the parties hereto shall bind and inure to the benefit of the respective successors and assigns of the parties hereto whether so expressed or not. In addition, whether or not any express assignment has been made, the provisions of this Agreement which are for the benefit of the Holders of Registrable Securities are also for the benefit of, and enforceable by, any subsequent holder of Registrable Securities. The registration rights provided in this

Agreement may be transferred without restriction and shall inure to and be enforceable by any and all Holders of Registrable Securities, including, without limitation, any successors, assigns, transferees, heirs, executors and administrators of the Investors.

19. Severability. Unless otherwise expressly provided herein, each Investor's or Holders 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.

20. Counterparts; Facsimile Transmission. This Agreement may be executed simultaneously in two or more counterparts, any one of which need not contain the signatures of more than one party, but all such counterparts taken together shall constitute one and the same Agreement. Each party to this Agreement agrees that it will be bound by its own facsimilied signature and that it accepts the facsimilied signature of each other party to this Agreement.

21. Descriptive Headings. 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.

22. 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, excluding to the greatest extent permitted by law any rule of law that would cause the application of the laws of any jurisdiction other than the State of New York.

23. Notices. All notices, demands or other communications to be given or delivered under or by reason of the provisions of this Agreement shall be in writing and shall be deemed to have been given when delivered personally to the recipient, sent to the recipient by reputable overnight courier service (charges prepaid) or 48 hours after deposited in the United States mail, certified or registered to the recipient by postage prepaid or by facsimile. Such notices, demands and other communications shall be sent to the Investors and to any Holder at the addresses indicated on the Schedule of Investors attached hereto and to the Company at the address of its corporate headquarters or to such other address or to the attention of such other Person as the recipient party has specified by prior written notice to the sending party.

[THIS SPACE INTENTIONALLY LEFT BLANK]

IN WITNESS WHEREOF, the parties have executed this Agreement as of the date first written above.

COMPANY

HALSEY DRUG CO., INC.

By: _____
Name: _____
Title: _____

WATSON

WATSON PHARMACEUTICALS, INC.

By: _____
Name: _____
Title: _____

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

_____
By: Srini Conjeevaram
Its: General Partner

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

_____
By: Bruce F. Wesson
Its: General Partner

CARE CAPITAL INVESTMENTS II, L.P.
By: Care Capital II, LLC, General Partner
47 Hulfish Street, Suite 310
Princeton, NJ 08542

_____
By: David R. Ramsay
Its: Authorized Signatory

MICHAEL WEISBROT
1136 Rock Creek Road
Gladwyne, Pennsylvania 19035

_____

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

_____

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

_____
By: Srini Conjeevaram
Its: General Partner

ESSEX WOODLANDS VENTURES FUND V, L.P.
By: Essex Woodlands Health Ventures V, L.L.C.,
Its General Partner
190 South LaSalle Street, Suite 2800
Chicago, IL 60603

_____
By: Immanuel Thangaraj
Its: Managing Director

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

_____

SUSAN WEISBROT
1136 Rock Creek Road
Gladwyne, Pennsylvania 19035

_____

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

_____

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

ROGER GRIGGS
c/o Tom Jennings
7300 Turfway Road
Suite 300
Florence, KY 41042

GEORGE E. BOUDREAU
222 Elbow Lane
Haverford, PA 19041

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

_____
By: Srini Conjeevaram
Its: General Partner

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

_____
By: Bruce F. Wesson
Its: General Partner

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

_____
By: Srini Conjeevaram
Its: General Partner

ALAN SMITH
21 Bedlow Avenue
Newport, Rhode Island 02840

_____

PATRICK COYNE
800 Merion Square Road
Gladwyne, PA 19035

_____

MICHAEL WEISBROT
1136 Rock Creek Road
Gladwyne, Pennsylvania 19035

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

_____

DENNIS ADAMS
120 Kynlyn Road
Radnor, Pennsylvania 19312

_____

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

By: Robert W. Baird
Its: Trustee

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

By: Connie Reicher
Its: Trustee

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

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

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

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By: Michael Reicher
Its: Trustee

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Ft. Jennings, Ohio 45844

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Warren, New Jersey 07059

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

_____
By: Varshah H. Shah
Its: Custodian

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

_____
By: Varshah H. Shah
Its: Custodian

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

_____

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

_____

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

_____
By: _____
Its: Trustee

KENNETH GIMBEL
2455 Montgomery Avenue
Highland Park, Ill. 60035

_____

JESSICA K. CLEMENS
c/o Halsey Drug Co., Inc.
695 North Perryville Rd.
Crimson Building #2
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_____

JAKE P. CLEMENS
c/o Halsey Drug Co., Inc.
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BROOKE EMILY REICHER
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_____

ALEC JOHN REICHER
c/o Halsey Drug Co., Inc.
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COURTNEY PAIGE REICHER
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DEANA REICHER
c/o Halsey Drug Co., Inc.
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MICHAEL K. REICHER II
c/o Halsey Drug Co., Inc.
695 North Perryville Rd.
Crimson Building #2
Rockford, Ill. 61107

TODD ALLEN REICHER
c/o Halsey Drug Co., Inc.
695 North Perryville Rd.
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Rockford, Ill. 61107

ORACLE STRATEGIC PARTNERS, L.P.
By: Oracle Strategic Capital L.L.C.,
General Partner
200 Greenwich Avenue
3rd Floor
Greenwich, CT 06830

_____
By: Joel Liffmann
Its: Authorized Agent

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

_____
By: Bruce F. Wesson
Its: General Partner

ALAN SMITH
21 Bedlow Avenue
Newport, Rhode Island 02840

_____

MICHAEL WEISBROT
1136 Rock Creek Road
Gladwyne, Pennsylvania 19035

_____

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

_____
By: Srini Conjeevaram
Its: General Partner

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Its: Custodian

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By: Varshah H. Shah
Its: Custodian

MICHAEL RAINISCH
c/o Alvin Rainisch
31 Congressional Road
Jackson, New Jersey 08527

ILENE RAINISCH
c/o Alvin Rainisch
35 Congressional Road
Jackson, New Jersey 08527

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

_____
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Its: General Partner

GALEN EMPLOYEE FUND III, L.P.
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By: Bruce F. Wesson
Its: General Partner

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New York, New York 10020

_____
By: Srini Conjeevaram
Its: General Partner

SCHEDULE 1

SCHEDULE OF INVESTORS

Watson:

Watson Pharmaceuticals, Inc.
311 Bonnie Circle
Corona, California 92880
Attention: Michael Boxer

Tel: _____
Fax: _____

2002 HOLDERS

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

Tel: _____
Fax: _____

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Tel: _____
Fax: _____

ESSEX WOODLANDS VENTURES FUND V, L.P.
By: Essex Woodlands Health Ventures V,
L.L.C., Its General Partner
190 South LaSalle Street, Suite 2800
Chicago, IL 60603

Tel: _____
Fax: _____

CARE CAPITAL INVESTMENTS II, LP

By: Care Capital II, LLC, as general
partner

Tel: _____
Fax: _____

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

Tel: _____
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GEORGE E. BOUDREAU
222 Elbow Lane
Havenford, PA 19041

Tel: _____
Fax: _____

ROGER GRIGGS
c/o Tom Griggs
7300 Turfway Road
Suite 300
Florence, KY 41042

Tel: _____
Fax: _____

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By: Claudius, L.L.C., General Partner
610 Fifth Avenue, 5th Floor
New York, New York 10020

Tel: _____
Fax: _____

SCHEDULE 2

BRIDGE LOAN WARRANTS

See attached.

DATE OF WARRANT	WARRANT EXERCISE PRICE	GALEN PARTNERS III, L.P.	GALEN PARTNERS INTERNATIONAL III, L.P.	GALEN EMPLOYEES FUND III, L.P.
August 12, 1998	$ 2.2100	47,646	4,611	209
September 17, 1998	$ 1.8900	23,824	2,305	104
October 2, 1998	$ 1.7300	23,824	2,305	104
October 19, 1998	$ 1.5000	7,147	692	31
October 19, 1998	$ 1.4700	35,735	3,459	156
November 6, 1998	$ 1.4700	71,471	6,917	311
December 2, 1998	$ 1.3000	654,098	59,208	2,679
March 8, 1999	$ 1.1400	64,120	5,804	262
May 3, 1999	$ 1.1200	11,863	1,073	49
January 7, 2000	$ 1.4000	23,965	2,169	99
January 21, 2000	$ 1.4300	47,931	4,339	196
February 19, 2000	$ 1.1300	23,965	2,169	99
March 4, 2000	$ 1.5500	23,965	2,169	99
August 15, 2001	$ 3.0120	140,459	12,715	576
January 9, 2002	$ 1.8370	146,157	13,230	598
January 9, 2002	$ 1.8370	66,805	6,047	273
February 1, 2002	$ 1.8700	68,518	6,202	280
March 1, 2002	$ 2.0870	68,518	6,202	280
April 1, 2002	$ 2.0100	45,678	4,135	187
May 8, 2002	$ 2.1600	1,635,580	148,044	6,696
May 8, 2002	$ 2.1600	548,142	49,614	2,244
May 8, 2002	$ 2.1600	241,586	21,867	989
June 3, 2002	$ 1.9000	215,194	19,478	881
July 23, 2002	$ 1.7200	186,772	16,905	765
July 23, 2002	$ 1.4500	82,220	7,442	337
August 5, 2002	$ 1.4200	151,245	13,690	619
September 3, 2002	$ 1.5100	121,808	11,025	499
October 1, 2002	$ 1.7545	93,386	8,453	382
November 4, 2002	$ 1.7565	11,775	1,066	48
November 12, 2002	$ 1.7730	10,151	919	42
November 21, 2002	$ 1.5770	24,971	2,260	102
		4,918,519	446,514	20,196

EXHIBIT 10.17

WARRANT RECAPITALIZATION AGREEMENT

This WARRANT RECAPITALIZATION AGREEMENT is dated as of December 20, 2002, between Halsey Drug Co., Inc., a New York corporation (the "Company"), and the Investors listed on the signature page of this Agreement (the "Investors").

W I T N E S S E T H :

WHEREAS, the Company desires to recapitalize (the "Recapitalization") 8,104,336 of the outstanding Warrants ("Warrants") to purchase one share of the Company's common stock, par value $.01 per share (the "Common Stock") into an aggregate of 5,938,520 shares of the Company's Common Stock and the Investors have agreed to participate in the Recapitalization on the terms and subject to the conditions set forth herein;

WHEREAS, the Company is a party to a certain Debenture Purchase Agreement dated of even date herewith with the Purchasers listed on the signature pages thereto providing for the Company's issuance of 5% convertible senior secured debentures due March 21, 2006 in the principal amount of up to $35 million (the "Purchase Agreement") and it is a condition to the completion of the transactions contemplated in the Purchase Agreement that the Recapitalization shall be completed in accordance with the terms of this Agreement;

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

SECTION 1. RECAPITALIZATION OF WARRANTS

(a) Subject to the terms and conditions hereof and in reliance upon the representations and warranties of the Company contained herein, each Investor agrees to tender to the Company on the Closing Date specified in Section 2 hereof, the number of Warrants set forth opposite such Investor's name on Schedule 1 hereto to be recapitalized for, and the Company agrees to issue and/or deliver to the Investor on the Closing Date, the number of shares of Common Stock in certificate form as set forth opposite such Investor's name on Schedule 1 hereto.

(b) Each of the Company and the Investors agrees that for purposes of calculating the number of shares of Common Stock issuable to the Investors for the Warrants described in Schedule 1 hereto, the definition of "Fair Market Value" as provided in Section 3(b) of each of the Warrants described on Schedule 1 is hereby amended and restated to provide as follows:

"Fair Market Value"

> shall mean the average of the closing bid and asked prices of the Common Stock in the over-the-counter market at the close of trading for each of the ten (10) consecutive trading days through and including December 4, 2002.

(c) The Company intends to treat the Recapitalization as a reorganization within the meaning of Section 368(a)(1) of the U.S. Internal Revenue Code of 1986, as amended.

SECTION 2. THE CLOSING

(a) Subject to the terms and conditions hereof, the closing of the Recapitalization (the "Closing") will take place at the offices of St. John & Wayne, L.L.C., Two Penn Plaza East, Newark, New Jersey 07105 at 10:00 a.m. local time on the earliest practicable date following satisfaction or waiver of the conditions set forth in Section 6 hereof and concurrent with the closing of the transactions contemplated in the Purchase Agreement. Such time and date are herein referred to as the "Closing Date".

(b) Subject to the terms and conditions hereof, on the Closing Date (i) the Company will deliver to each Investor a certificate registered in such Investor's name (or the name of its nominee, if any, as specified on Schedule 1 hereto) evidencing the number of shares of Common Stock set forth opposite such Investor's name on Schedule 1 hereto, and (ii) the Investor will deliver to the Company certificates evidencing the number of Warrants set forth opposite such Investor's name on Schedule 1 hereto.

SECTION 3. REPRESENTATIONS AND WARRANTIES OF THE COMPANY

The Company represents and warrants to the Investors as follows as of the date hereof and as of the Closing Date:

3.1 Corporate Power and Authority.

The Company is duly organized, validly existing and in good standing under the laws of the State of New York. The Company has all requisite corporate power and authority to enter into and deliver this Agreement and to perform its obligations hereunder and to consummate the transactions contemplated by this Agreement. The execution, delivery and performance of this Agreement by the Company have been duly authorized by all necessary corporate action on the part of the Company. This Agreement has been duly executed and delivered by the Company and (assuming due authorization, execution and delivery by each Investor) constitutes the legal, valid and binding obligation of the Company enforceable against the Company in accordance with its terms subject to (a) applicable bankruptcy, insolvency, fraudulent conveyance and other similar laws, and (b) general principles of equity, including equitable defenses and limits as to the availability of equitable remedies, whether such principles are considered in a proceeding at law or in equity.

3.2 Capitalization of the Company.

As of the date of this Agreement, the Company's authorized capital stock consists solely of 80,000,000 shares of Common Stock, of which 15,065,240 shares are outstanding and 66,037,354 shares are reserved for issuance upon conversion of outstanding convertible debentures, common stock purchase warrants and stock options. All of the issued and outstanding shares of capital stock of the Company (i) have been duly authorized and validly

issued, (ii) are fully paid and non-assessable and (iii) have been offered, issued, sold and delivered by the Company in compliance with applicable Federal and state securities laws.

3.3 Conflicts; Consents and Approvals.

The execution and delivery of this Agreement and the consummation of the transactions contemplated by this Agreement do not and will not (a) violate, conflict with, or result in a breach of any provision of, or constitute a default under, the Company's Certificate of Incorporation, as amended, or By-laws; (b) violate, or conflict with, or result in a breach of any provision of, or constitute a default (or an event which, with the giving of notice or lapse of time or both, would become a default) under, or entitle any party to terminate, accelerate, modify or cause a default under, or result in the creation of any encumbrance or lien upon any of the properties or assets of the Company under, any of the terms, conditions or provisions of any note, bond, mortgage, indenture, deed of trust, license, contract, undertaking, agreement, lease or other instrument or obligation to which the Company is a party; (c) violate any order, writ, injunction, decree, statute, rule or regulation applicable to the Company; or (d) other than required filings with the Securities and Exchange Commission (the "Commission") or with state securities regulators pursuant to state securities or "blue sky" laws, require any action or consent or approval of, or review by, or registration or material filing by the Company with, any third party or any local, state or federal court, arbitral tribunal, administrative agency or commission or other governmental or regulatory body, agency, instrumentality or authority, except, with respect to clauses (b), (c) and (d), as would not have a material adverse effect on the Company.

3.4 Board Recommendation.

In accordance with the applicable provisions of the New York Business Corporation Law and the Company's Certificate of Incorporation, as amended, and By-laws, the Board of Directors of the Company, at a meeting duly called and held, at which a quorum was present throughout, upon the recommendation of an independent committee of the Board of Directors, has adopted a resolution proposing and declaring the advisability of this Agreement and the transactions contemplated hereby.

3.5 Litigation.

As of the date immediately preceding the date hereof, to the Company's knowledge, there are no actions, suits or proceedings pending against the Company (or any of its properties, rights or franchises), at law or in equity, or before any federal or state commission, board, bureau, agency, regulatory or administrative instrumentality or other governmental authority or any arbitrator or arbitration tribunal, that would be reasonably expected to, individually or in the aggregate, prevent, materially impair or materially delay the consummation of the transactions contemplated hereby.

3.6 Other Information.

Since December 31, 2001, except as disclosed on Schedule 2 hereto or in the Company's quarterly reports on Form 10-Q for the quarter and nine months ended September 30, 2002, (a)

the business of the Company has been conducted in the ordinary course, and (b) there have been no material adverse changes in the assets, properties, liabilities, business, affairs, results of operations, condition (financial or otherwise) or prospects of the Company. There are no material liabilities of the Company which would be required to be provided for in a consolidated balance sheet of the Company prepared in accordance with United States generally accepted accounting principles consistently applied, other than liabilities provided for in the historical financial statements included in the Company's filings with the Commission pursuant to the Securities Exchange Act of 1934, as amended (the "Exchange Act.").

3.7 SEC Reports.

The Company has filed all proxy statements, reports and other documents required to be filed by it under the Exchange Act. The Company has furnished each Investor with copies of (a) its Annual Report on Form 10-K for the fiscal year ended December 31, 2001, (b) its Quarterly Report on Form 10-Q for the quarter and nine months ended September 30, 2002, and (c) its Proxy Statement dated May 7, 2001 (collectively, the "SEC Reports"). Each SEC Report was in substantial compliance with the requirements of its respective form and none of the SEC Reports, nor the financial statements (and the notes thereto) included in the SEC Reports, as of their respective dates or as subsequently supplemented or amended, contained any untrue statement of a material fact or omitted to state a material fact required to be stated therein or necessary to make the statements therein, in light of the circumstances under which they were made, not misleading.

SECTION 4. REPRESENTATIONS AND WARRANTIES OF THE INVESTORS

Each Investor, on a several and not joint basis, represents and warrants to the Company as follows as of the date hereof and as of the Closing Date:

4.1 Corporate Power and Authority.

The Investor has all requisite power, authority and legal right to execute, deliver, enter into, consummate the transactions contemplated by and perform its obligations under this Agreement. The execution, delivery and performance of this Agreement by the Investor have been duly authorized by all required corporate and other actions. The Investor has duly executed and delivered this Agreement and this Agreement constitutes the legal, valid and binding obligations of the Investor enforceable against the Investor in accordance with its terms, subject to bankruptcy, insolvency, reorganization, moratorium, fraudulent transfer and other similar laws relating to the rights of creditors generally from time to time in effect, to general principles of equity, including without limitation, concepts of materiality, reasonableness, good faith and fair dealing, regardless of whether in a proceeding in equity or at law.

4.2 Investment Intent.

The Investor is acquiring the Common Stock to be delivered in the Recapitalization for its own account for investment and not with a view to, or for resale in connection with, any distribution thereof in violation of applicable securities laws; provided, however, that the Investor may

transfer record and/or beneficial ownership of the Common Stock to one or more affiliates, officers or employees of affiliates so long as the transfer is made in compliance with the Securities Act of 1933, as amended (the "Securities Act"), and applicable state laws. The Investor understands that none of the Common Stock to be received in the Recapitalization has been registered under the Securities Act. If the Investor should in the future decide to dispose of any of its Common Stock, it is understood that it may do so only in compliance with the Securities Act, applicable securities laws and this Agreement. The Investor is an "accredited investor" as defined in Rule 501(a) under the Securities Act.

4.3 Access.

The Investor has had access to such financial and other information, and has been afforded the opportunity to ask such questions of representatives of the Company, including the Chairman and the Chief Financial Officer, and receive answers with respect thereto, as the Investor deems necessary in connection with its decision to participate in the Recapitalization.

4.4 Investor Qualification.

(a) The Investor owns the Warrants set forth opposite the Investor's name in Schedule 1 hereto.

(b) The Investor (alone or with the aid of its investment advisors) has such knowledge and experience in financial and business matters that the Investor is capable of evaluating the merits and risks of its investment in the Common Stock.

(c) The Investor is able to bear the economic risk of an investment in the Common Stock and has the ability to hold the Common Stock to be acquired by such Investor indefinitely and the ability to suffer a complete loss of such investment.

(d) The Investor is familiar with the type of investment which the Common Stock constitutes and has reviewed the investment in the Common Stock subscribed herein with tax and legal counsel and investment representatives to the extent deemed advisable. The Investor believes that the Common Stock and the amount of such Investor's investment are consistent with such Investor's overall investment program and financial position.

(e) All information the Investor has supplied to the Company is true and accurate.

(f) The Investor will immediately notify the Company if any of the representations and warranties made herein become untrue.

SECTION 5. TRANSFER OF SECURITIES

5.1 Restrictions.

Each Investor agrees that it will not sell or otherwise dispose of any Common Stock, unless such Common Stock shall have been registered under the Securities Act and, to the extent required,

under any applicable state securities laws, or pursuant to an applicable exemption from such registration requirements. The Company may endorse on all certificates evidencing the Common Stock a legend stating or referring to such transfer restrictions and require, as a condition to transfer, from such Investor and any proposed transferee of such Investor, such certifications, legal opinions or other information as the Company may reasonably require to confirm that such transfer is being made in compliance with, pursuant to an exemption from, or in a transaction not subject to, the registration requirements of the Securities Act or any state securities laws; provided, however, that no such legend shall be endorsed on any such certificates which, when issued, are no longer subject to the restrictions of this Section 5.

SECTION 6. CONDITIONS PRECEDENT

6.1 Conditions to Each Party's Obligation.

The respective obligation of each party to effect the Recapitalization shall be subject to the condition that no statute, rule, regulation, executive order, decree, temporary restraining order, preliminary or permanent injunction or other order issued by any court of competent jurisdiction or other governmental entity or other legal restraint or prohibition preventing the consummation of the Recapitalization shall be in effect; provided, however, that each of the parties shall have used reasonable efforts to prevent the entry of any such injunction or other order and to appeal as promptly as possible any injunction or other order that may be entered.

6.2 Conditions to the Company's Obligation.

The obligation of the Company to effect the Recapitalization shall be subject to the satisfaction at or prior to the Closing Date of the following additional conditions (any of which may be waived by the Company): (a) Each of the Investors shall have performed in all material respects each of its agreements contained in this Agreement required to be performed at or prior to the Closing Date, and (b) each of the representations and warranties of each of the Investors contained in this Agreement shall be true and correct in all material respects on and as of the Closing Date as if made on and as of such date (other than to the extent that any such representation and warranty, by its terms, is expressly limited to a specific date, in which case such representation and warranty shall be true and correct in all material respects as of such date).

6.3 Conditions to the Investors' Obligations.

The obligation of the Investors to effect the Recapitalization shall be subject to the satisfaction at or prior to the Closing Date of the following additional conditions (any of which may be waived by such Investor): (a) The Company shall have performed in all material respects each of its agreements contained in this Agreement required to be performed at or prior to the Closing Date, and (b) each of the representations and warranties of the Company contained in this Agreement shall be true and correct in all material respects on and as of the Closing Date as if made on and as of such date (other than to the extent that any such representation and warranty, by its terms, is expressly limited to a specific date, in which case such representation and warranty shall be true and correct in all material respects as of such date).

SECTION 7. INDEMNIFICATION

(a) The representations, warranties, covenants and agreements of the Company and the Investors contained in this Agreement or in any document or certificate delivered pursuant hereto or thereto or in connection herewith shall survive, and shall continue in effect following, the execution and delivery of this Agreement and the Closing for a period of two (2) years from the date of this Agreement.

(b) The Company agrees to indemnify and hold the Investors harmless from and against any loss, damage, liability or expense (including amounts paid in settlement and reasonable attorneys' fees and expenses) to the Investors resulting from any breach of the representations, warranties, covenants or agreements of the Company contained in this Agreement or any other document or certificate delivered by the Company pursuant hereto or thereto or in connection herewith or therewith; provided, however, that the Company shall not be required to indemnify the Investors for any diminution in the value of the Common Stock.

SECTION 8. MISCELLANEOUS

8.1 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, excluding to the greatest extent permitted by law any rule of law that would cause the application of the laws of any jurisdiction other than the State of New York.

8.2 Specific Performance.

The transactions contemplated by this Agreement are unique. Accordingly, each of the parties acknowledges and agrees that, in addition to all other remedies to which it may be entitled, each of the parties hereto is entitled to a decree of a specific performance and injunctive and other equitable relief.

8.3 Amendments and Waiver.

The terms and provisions of this Agreement may be amended, waived, modified or terminated only with the written consent of (1) the Company, and (2) the holders of two-thirds of the outstanding Warrants; provided, however, that no such amendment, waiver, modification or termination shall change this Section 8.4 without the written consent of all of the Investors then holding Warrants.

8.4 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 parties hereto and their respective successors, assigns, heirs, executors and administrators. No party may assign any of its rights

hereunder without the prior written consent of the other parties; provided, however, that any Investor may assign any of its rights under this Agreement to any affiliate of such Investor.

8.5 Entire Agreement.

This Agreement (including the 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.

8.6 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 an Investor, to the address set forth on the signature pages 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 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.

8.7 Delays or Omissions.

No delay or omission to exercise any right, power or remedy accruing to any party to this Agreement upon any breach or default of any other party to this Agreement shall impair any such right, power or remedy of such party 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 party 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 party, shall be cumulative and not alternative.

8.8 Independence of Covenants and Representations and Warranties.

All covenants hereunder shall be given independent effect so that if a certain action or condition constitutes a default under a certain covenant, the fact that such action or condition is permitted by another covenant shall not affect the occurrence of such default. In addition, all representations and warranties hereunder shall be given independent effect so that if a particular representation or warranty proves to be incorrect or is breached, the fact that another representation or warranty concerning the same or similar subject matter is correct or is not breached will not affect the incorrectness of or a breach of a representation and warranty hereunder.

8.9 Rights and Obligations; Severability.

Unless otherwise expressly provided herein, each Investor'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.

8.10 Expenses.

All costs and expenses incurred in connection with this Agreement and the transactions contemplated by this Agreement shall be the responsibility of and shall be paid by the party incurring such fees and expenses, whether or not the transactions contemplated by this Agreement are consummated.

8.11 Jurisdiction.

(a) Each of the parties hereto hereby irrevocably and unconditionally submits, for itself and its property, to the nonexclusive jurisdiction of any New York State court or United States Federal court sitting in New York City, and any appellate court from any thereof, in any action or proceeding arising our of or relating to this Agreement or for recognition or enforcement of any judgment, and each of the parties hereto irrevocably and unconditionally agrees that all claims in respect of any such action or proceeding may be heard and determined in any such New York State court or, to the fullest extent permitted by law, in such United States Federal court. Each of the parties hereto agrees that a final judgment in any such action or proceeding shall be conclusive and may be enforced in other jurisdictions by suit on the right that any party may otherwise have to bring any action or proceeding relating to this Agreement in the courts of any other jurisdiction.

(b) Each of the parties hereto irrevocably and unconditionally waives, to the fullest extent it may legally and effectively do so, any objection that it may now or hereafter have to the laying of venue of any suit, action or proceeding arising out of or in relation to this Agreement in

any such New York State or United States Federal court sitting in New York City. Each of the parties hereto hereby irrevocably waives, to the fullest extent permitted by law, the defense of an inconvenient forum to the maintenance of such action or proceeding in any such court.

8.12 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.

8.13 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.

8.14 Waiver of Jury Trial.

EACH OF THE PARTIES HERETO HEREBY IRREVOCABLY WAIVES ALL RIGHT TO TRIAL BY JURY IN ANY ACTION, PROCEEDING OR COUNTERCLAIM (WHETHER BASED ON CONTRACT, TORT OR OTHERWISE) ARISING OUT OF OR RELATING TO THIS AGREEMENT OR THE ACTIONS OF ANY PARTY IN THE NEGOTIATION, ADMINISTRATION, PERFORMANCE OR ENFORCEMENT HEREOF.

IN WITNESS WHEREOF, the parties hereto have caused this Agreement to be executed as of the date first above written.

HALSEY DRUG CO., INC.

By:_____
Name: _____
Title: _____

INVESTORS

ORACLE STRATEGIC PARTNERS, L.P.
By: Oracle Strategic Capital L.L.C.,
General Partner
200 Greenwich Avenue
3rd Floor
Greenwich, CT 06830

_____
By: Joel Liffmann
Its: Authorized Agent

DANIEL HILL
6725 Lynch Avenue
Riverbank, CA 95367

_____

ALAN SMITH
21 Bedlow Avenue
Newport, Rhode Island 02840

_____

PATRICK COYNE
800 Merion Square Road
Gladwyne, PA 19035

_____

MICHAEL WEISBROT
1136 Rock Creek Road
Gladwyne, Pennsylvania 19035

_____

SUSAN WEISBROT
1136 Rock Creek Road
Gladwyne, Pennsylvania 19035

_____

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

_____

DENNIS ADAMS
120 Kynlyn Road
Radnor, Pennsylvania 19312

_____

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

_____

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

_____
By: Michael K. Reicher
Its: Trustee

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

_____
By: Connie Reicher
Its: Trustee

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

_____

KENNETH GIMBEL
2455 Montgomery Avenue
Highland Park, Ill. 60035

_____

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

_____

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

_____

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

_____

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

_____
By: Varshah H. Shah
Its: Custodian

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

_____
By: Varshah H. Shah
Its: Custodian

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

_____

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

_____

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

_____
By: Robert W. Baird
Its: Trustee

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

_____
By: Robert W. Baird
Its: Trustee

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

_____
By: Michael K. Reicher
Its: Trustee

SCHEDULE 1

INVESTOR WARRANTS

EXHIBIT 99.1

Contact: Halsey Pharmaceuticals
Investor Relations - Peter A. Clemens, Vice President & CFO
(815) 399-2060

FOR IMMEDIATE RELEASE

HALSEY PHARMACEUTICALS ANNOUNCES COMPLETION OF FINANCING

ROCKFORD, IL, DECEMBER 23, 2002: Halsey Pharmaceuticals (OTC.BB-HDGC) today announced that it has completed a private offering of 5% convertible senior debentures in the aggregate principal amount of approximately $26,385,000. The lead investors in the offering were Essex Woodlands Health Ventures, Care Capital LLC and Galen Partners III. A portion of this financing represents the conversion of the Company's outstanding $15 million bridge loans and accrued interest thereon into the new Debentures. The terms of the offering provide for additional investors in an amount that would raise the total aggregate principal amount of the offering to $35,000,000.

The new Debentures, which mature at March 31, 2006, are convertible into shares of the Company's Common Stock at a price of $.34 per share and represent a fully-diluted ownership interest of approximately 36% of the Company.

The Company intends to use the funds to proceed with development of its proprietary opiate technology for use in the manufacture of controlled substance active pharmaceutical ingredients as well as finished dosage products for pain management.

As part of the offering, the Company recapitalized warrants to purchase 8,145,736 shares into 5,970,083 shares of the Company's Common Stock. As a result, the Company's outstanding shares of Common Stock increased to 21,035,323 shares. Additionally, the Company restructured the terms of its outstanding convertible debentures to extend the maturity date of such debentures from March 15, 2003 to March 31, 2006.

As a condition to the completion of the Debenture offering, the Company and Watson Pharmaceuticals amended the terms of the Watson Term Loan Agreement with the Company to (i) include in the principal amount of the Watson Term Loan the Company's outstanding payment obligation to Watson of approximately $4 million under a product supply agreement between the parties, and (ii) extend the maturity date of the Watson Term Loan from March 31, 2003 to March 31, 2006. In consideration for the amendments to the Watson Term Loan Agreement, the Company issued to Watson a common stock purchase warrant exercisable for 10,700,665 shares of the Company's Common Stock at an exercise price per share equal to the conversion price of the new Debentures.

After giving effect to the issuance of the new Debentures, the Watson Warrant, the warrant recapitalization and the dilution protection provisions in the Company's outstanding debentures and warrants, the Company has outstanding securities convertible into an aggregate of approximately 201,390,000 shares of the Company's Common Stock.

Commenting, Michael Reicher, Chairman & CEO said, "We see tremendous opportunities in our areas of strategic focus concentrating on pain management and are delighted that Essex Woodlands Health Ventures and Care Capital LLC as well as Galen Partners have demonstrated confidence in our business model by making this investment".

Halsey Pharmaceuticals, together with its subsidiaries, is an emerging pharmaceutical company specializing in innovative drug development.

The statements in this press release are forward looking and are made pursuant to the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. Investors are cautioned that forward looking statements involve risk and uncertainties which may affect Halsey's business prospects, including economic, competitive, governmental, technological and other factors discussed in filings with the Securities and Exchange Commission.

This and past press releases for Halsey Pharmaceuticals are available at the Company's web site at WWW.HALSEYDRUG.COM.