

---

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

---

**FORM 10-K**

---

**ANNUAL REPORT PURSUANT TO  
SECTIONS 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

(Mark One)

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

For the fiscal year ended December 31, 2006

Or

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

Commission file number 001-13341

---

**TITAN PHARMACEUTICALS, INC.**

(Exact name of registrant as specified in its charter)

---

**Delaware**  
(State or other jurisdiction of  
incorporation or organization)

**94-3171940**  
(I.R.S. Employer  
identification number)

**400 Oyster Point Blvd., Suite 505,  
South San Francisco, California**  
(Address of principal executive offices)

**94080**  
(Zip code)

**Registrant's telephone number, including area code: (650) 244-4990**

**Securities registered pursuant to Section 12(b) of the Act:**

Title of each class  
**Common Stock, \$.001 par value**

Name of each exchange on which registered  
**The American Stock Exchange**

**Securities registered pursuant to Section 12(g) of the Act: None**

---

Indicate by check mark if the registrant is a well-known seasoned issuer as defined in Rule 405 of the Securities Act. Yes  No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Exchange Act. Yes  No

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

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§ 229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition or "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer  Accelerated filer  Non-accelerated filer

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes  No

The aggregate market value of the 38,004,728 shares of voting and non-voting common equity held by non-affiliates of the registrant based on the closing price on June 30, 2006 was \$81.3 million.

As of March 1, 2007, 39,029,440 shares of common stock, \$.001 par value, of the registrant were issued and outstanding.

**DOCUMENTS INCORPORATED BY REFERENCE: NONE**

---

## PART I

Statements in this Form 10-K that are not descriptions of historical facts are forward-looking statements that are subject to risks and uncertainties. Actual results could differ materially from those currently anticipated due to a number of factors, including those set forth under “Risk Factors” including, but not limited to, the results of research and development efforts, the results of pre-clinical and clinical testing, the effect of regulation by the United States Food and Drug Administration (FDA) and other agencies, the impact of competitive products, product development, commercialization and technological difficulties, the Company’s ability to obtain additional financing, the effect of our accounting policies, and other risks detailed in our Securities and Exchange Commission filings.

Probuphine®, Spheramine®, ProNeura™ and CCM™ are trademarks of Titan Pharmaceuticals, Inc. This Form 10-K also includes other trade names and trademarks of companies other than Titan Pharmaceuticals, Inc.

References herein to “we,” “us,” “Titan,” and “our company” refer to Titan Pharmaceuticals, Inc. and its subsidiaries unless the context otherwise requires.

### Item 1. Business

#### (a) General Development of Business

We are a biopharmaceutical company developing proprietary therapeutics for the treatment of central nervous system (CNS) disorders, cardiovascular disease, bone disease and other disorders. Our product development programs focus primarily on large pharmaceutical markets with significant unmet medical needs and commercial potential. We are focused primarily on clinical development of the following products:

- Probuphine: for the treatment of opioid dependence
- Iloperidone: for the treatment of schizophrenia and related psychotic disorders (partnered with Vanda Pharmaceuticals, Inc.)
- Spheramine: for the treatment of advanced Parkinson’s disease (partnered with Bayer Schering Pharma AG)
- DITPA: for the treatment of cardiovascular disease
- Gallium maltolate: for the treatment of bone related diseases, chronic bacterial infections and cancer

We are directly developing our product candidates and also utilizing corporate partnerships, including a collaboration with (i) Bayer Schering Pharma AG, Germany (Bayer Schering) for the development of Spheramine to treat Parkinson’s disease, and (ii) Vanda Pharmaceuticals, Inc. (Vanda) for the development of iloperidone for the treatment of schizophrenia and related psychotic disorders. We also utilize grants from government agencies to fund development of our product candidates.

---

## [Index to Financial Statements](#)

### (b) Financial Information About Industry Segments

We operate in only one business segment, the development of pharmaceutical products.

### (c) Narrative Description of Business

#### Product Development Programs

The following table provides summary status of our products in development:

<u>Product</u>	<u>Potential Indication(s)</u>	<u>Phase of Development</u>	<u>Marketing Rights</u>
Probuphine	Opioid dependence	Phase III	Titan
Iloperidone	Schizophrenia, psychosis	Phase III	Vanda Pharmaceuticals, Inc.
Spheramine	Parkinson's disease	Phase IIb	Bayer Schering Pharma AG
DITPA	Hyperlipidemia	Phase II	Titan
Gallium maltolate	Bone related disease, chronic bacterial infections, cancer	Phase I	Titan

Our products are at various stages of development and may not be successfully developed or commercialized. We do not currently have any products being commercially sold. Our proposed products will require significant further capital expenditures, development, testing, and regulatory clearances prior to commercialization. We may experience unanticipated problems relating to product development and cannot predict whether we will successfully develop and commercialize any products.

#### Probuphine

We are developing Probuphine for the treatment of opioid dependence. Probuphine is the first product to utilize our novel, proprietary ProNeura long-term drug delivery technology (See "ProNeura Continuous Drug Delivery Technology" below). Probuphine is designed to provide continuous, long-term therapeutic levels of the drug buprenorphine, an approved agent for the treatment of opioid dependence.

In October 2006, we initiated a randomized, double-blind, placebo-controlled, multi-center Phase III clinical study of Probuphine in the treatment of opioid dependence. This 150 patient study, which is being conducted in the U.S., will evaluate the safety and effectiveness of treatment with Probuphine versus placebo in reducing opioid dependence over 24 weeks of treatment. This study is part of a registration directed program intended to obtain marketing approval of Probuphine for the treatment of opioid addiction in Europe and the U.S. The Phase III program includes additional clinical studies to be conducted later in the U.S. and Europe. We continue to have discussions with the U.S. Food and Drug Administration (FDA) relating to finalizing the Probuphine development program.

In June 2004, we announced final results from a pilot clinical study that evaluated the safety, pharmacokinetics and preliminary efficacy of Probuphine in the treatment of opioid-dependent patients. The results were presented at the Annual Meeting of The International Society of Addiction Medicine in Helsinki, and demonstrated that all 12 patients switched from daily sublingual buprenorphine therapy to Probuphine, had maintenance of therapeutic benefit for a period of six months following a single treatment of Probuphine. Treatment with Probuphine was well tolerated in this clinical study, with no significant adverse events.

#### Iloperidone

Iloperidone is our novel, proprietary product in development for the treatment of schizophrenia and related psychotic disorders. Iloperidone was evaluated in a Phase III program comprising over 3,500 patients at more than 200 sites in 24 countries, administered and funded by Novartis Pharma AG (Novartis). In three completed efficacy studies conducted by Novartis, iloperidone statistically significantly reduced the symptoms of schizophrenia compared to placebo. Iloperidone has also been investigated in three 12-month safety studies, which confirm safety and tolerability. A dose dependent increase in the QTc interval was observed and investigated further in a clinical study, and no clinically significant adverse events were observed.

In June 2004, Vanda Pharmaceuticals, Inc. (Vanda) acquired from Novartis the worldwide rights to develop and commercialize iloperidone. Vanda was founded by Dr. Argeris N. Karabelas, former CEO of Novartis Pharmaceuticals, and Dr. Mihael Polymeropoulos, former Vice President of Pharmacogenetics at Novartis Pharmaceuticals. All of our rights and economic interests in iloperidone, including royalties on sales of iloperidone, remain essentially unchanged under the agreement.

---

## [Index to Financial Statements](#)

In December 2006, Vanda announced positive results from a Phase III clinical trial evaluating iloperidone in patients with schizophrenia. In this study, iloperidone demonstrated statistically significant improvement compared to placebo on the Positive and Negative Symptom Scale (PANSS), the trial's primary endpoint. Iloperidone also achieved significant efficacy on the positive and negative symptom subscales of PANSS. The Phase III trial was a randomized, double-blind, placebo-controlled, multi-center, 4 week study that enrolled 604 patients with schizophrenia. The trial evaluated 12 mg of iloperidone dosed twice-daily (24 mg per day). The primary endpoint was efficacy vs. placebo in PANSS (total) and was determined using the Mixed Method Repeated Measures (MMRM) methodology. The safety profile of iloperidone was consistent with what has been observed in previous iloperidone Phase III trials.

Iloperidone's efficacy and safety was also evaluated in this study in patients with specific genetic profiles using pharmacogenetics, in order to potentially give physicians and patients information to potentially help individualize their antipsychotic therapy. It had been previously identified that a certain polymorphism in a gene, occurring in approximately 70% of patients, may be associated with the pathogenesis of schizophrenia and appeared to correlate with iloperidone response. Iloperidone achieved statistical significance vs. placebo on the PANSS scale in these patients, with a magnitude of response greater than that seen in the overall iloperidone population.

Vanda plans to file a New Drug Application (NDA) with the FDA for iloperidone by the end of 2007.

### **Spheramine**

Spheramine is a cell-based therapeutic being developed for the treatment of advanced Parkinson's disease. It utilizes our proprietary cell-coated microcarrier (CCM) technology, which enables the development of cell-based therapies for minimally-invasive, site-specific delivery to the central nervous system of therapeutic factors precisely where they are needed.

Spheramine consists of microcarriers coated with human retinal pigment epithelial cells that are intended to enhance brain levels of dopamine, a neurotransmitter deficient in certain brain regions in Parkinson's disease, leading to movement disorders. Preclinical studies have demonstrated the preliminary efficacy and safety of Spheramine, including blinded studies in a primate model of Parkinson's disease. Positron emission tomography (PET) imaging studies in primates have confirmed the presence of increased dopamine signals in regions treated with Spheramine. A pilot clinical study of Spheramine performed by Titan in six patients with advanced Parkinson's disease demonstrated substantial improvement (average 48%) in motor function at one-year post treatment with no significant adverse events. These results were first reported at the American Academy of Neurology (AAN) annual meeting in 2002. In June 2005, Bayer Schering sponsored a symposium on Spheramine at the International Congress on Parkinson's Disease and Related Disorders in Berlin. In the keynote address, Ray Watts, M.D., Professor and Chairman, Department of Neurology, University of Alabama Birmingham, presented 48-month follow-up data for the six patients in our pilot clinical study of Spheramine. The data presented indicate that Spheramine is well tolerated and that patients continued to demonstrate 43% average improvement in motor function over baseline, four years after treatment.

Spheramine is currently being studied in an ongoing multicenter, randomized, double-blind, placebo controlled clinical trial in Parkinson's disease. This Phase IIb clinical study will enroll 68 patients with advanced Parkinson's disease (Hoehn and Yahr Stages III and IV) to further evaluate the efficacy, safety, and tolerability of Spheramine. To date 65 patients have been treated and the results from this study are expected to be available in 2008.

Bayer Schering, our corporate partner for worldwide development and commercialization of Spheramine, is funding the clinical development program for Spheramine. Under this agreement, Bayer Schering received exclusive, worldwide development, manufacturing and commercialization rights, and, in addition to the clinical and manufacturing development funding and milestone payments, Bayer Schering will pay us a royalty on future product sales. The Investigational New Drug application (IND) filed by Titan with the FDA was transferred to Bayer Schering in November 2005.

In July 2004, we announced that the FDA had granted a Fast Track designation for Spheramine for the treatment of advanced Parkinson's disease. The Fast Track Program is designed by the FDA to facilitate the development and expedite the review of drug candidates that demonstrate the potential to treat serious or life-threatening diseases and address unmet medical needs. The FDA had previously approved Orphan Drug designation for Spheramine for the treatment of advanced Parkinson's disease.

### **DITPA**

Our novel, proprietary product in development for the treatment of cardiovascular disease is 3,5-diiodothyropropionic acid, or DITPA, an orally active analogue of thyroid hormone.

---

## [Index to Financial Statements](#)

DITPA represents a potential new class of agents for cardiovascular disease, based upon the central role of thyroid hormone in regulating cardiovascular function.

We are currently evaluating DITPA as a potential treatment for hyperlipidemia in a Phase II, randomized, double-blind, placebo-controlled study at the Johns Hopkins Medical Institutions in Baltimore. The study includes individuals receiving standard lipid-lowering therapy, whose LDL cholesterol levels are above National Cholesterol Education Program (NCEP) guidelines. The study will evaluate DITPA as a cholesterol lowering agent in combination with standard therapy. Recent data have indicated that further lowering of target LDL cholesterol level guidelines may be important in reducing the incidence of heart disease and stroke. Accordingly, the NCEP has recently updated its guidelines to recommend that doctors target lower LDL cholesterol levels in their patients.

In October 2006, we determined to focus our resources on the Phase III development of Probuphine, and have discontinued further enrollment in our Phase II study of DITPA in congestive heart failure (CHF). We will subsequently analyze data collected to date.

In addition to the discontinuation of our Phase II clinical study in CHF, the Department of Veteran's Affairs has indicated that it will discontinue its Cooperative Studies Program Phase II study of DITPA in CHF patients.

### **Gallium Maltolate**

Gallium maltolate is our novel oral agent for the potential treatment of chronic bacterial infections, bone disease, and cancer. Gallium deprives bacteria of iron required for growth and renders resistant bacteria in biofilms susceptible to treatment. Gallium acts upon bone by enhancing the formation of osteoblasts and inhibiting osteoclasts, thereby increasing bone deposition and reducing bone turnover. Additionally, gallium also inhibits ribonucleotide reductase, a key enzyme essential for DNA replication in cancer cells.

In preclinical studies with an animal model for persistent infection due to bacterial biofilms, oral dosing of gallium maltolate was effective in eradicating infection in a dose dependent manner. Based on these results, we believe that gallium maltolate may have potential in the treatment of chronic bacterial biofilm-based infections, including lung infections associated with cystic fibrosis or urinary tract infections.

Prior independent studies using intravenously administered gallium nitrate have demonstrated preliminary evidence of clinical activity in several cancers, including multiple myeloma, lymphoma, bladder cancer and prostate cancer. An intravenous formulation of gallium nitrate, received FDA approval in 1991 for the treatment of hypercalcemia of malignancy.

In 2005, we completed a dose ranging Phase I clinical study of gallium maltolate in cancer patients. Significant blood levels of gallium were achieved, and a maximum tolerated dose level was not reached in this study. We are developing a new formulation of gallium maltolate with potentially improved bioavailability, and plan to use this formulation in any future clinical development of gallium maltolate.

### **ProNeura Continuous Drug Delivery Technology**

Our ProNeura continuous drug delivery system consists of a small, solid rod made from a mixture of ethylene-vinyl acetate (EVA) and a drug substance. The resulting product is a solid matrix that is placed subcutaneously, normally in the upper arm in a simple office procedure, and is removed in a similar manner at the end of the treatment period. The drug substance is released slowly, at continuous levels, through the process of diffusion. This results in a constant rate of release similar to intravenous administration. We believe that such long-term, linear release characteristics are desirable by avoiding peak and trough level dosing that poses problems for many CNS and other therapeutic agents.

In addition to Probuphine, which is our first product in clinical testing to utilize our proprietary ProNeura long term drug delivery technology, we are planning to develop our ProNeura sustained drug delivery technology for other potential treatment applications in which conventional treatment is limited by variability in blood drug levels and poor patient compliance. ProNeura technology was developed to address the need for a simple, practical method to achieve continuous long-term drug delivery, and potentially can provide controlled drug release on an outpatient basis over extended periods up to 6 – 12 months.

### **Sponsored Research and License Agreements**

We are a party to several agreements with research institutions, companies, universities and other entities for the performance of research and development activities and for the acquisition of licenses relating to such activities.

---

## [Index to Financial Statements](#)

### **Iloperidone**

In January 1997, we acquired an exclusive worldwide license under U.S. and foreign patents and patent applications relating to the use of iloperidone for the treatment of psychiatric and psychotic disorders and analgesia from Sanofi-Aventis SA (Sanofi-Aventis) (formerly Hoechst Marion Roussel, Inc.). The Sanofi-Aventis agreement provides for the payment of royalties on future net sales and requires us to satisfy certain other terms and conditions in order to retain our rights, all of which have been met to date.

In November 1997, we granted a worldwide sublicense, except Japan, to Novartis under which Novartis will continue, at its expense, all further development of iloperidone. In April 2001, that sublicense was extended to include Japan. Novartis will make our milestone and royalty payments to Sanofi-Aventis during the life of the Novartis agreement, and will also pay Titan a royalty on future net sales of the product.

In June 2004, Vanda acquired from Novartis the worldwide rights to develop and commercialize iloperidone. Under its agreement with Novartis, Vanda is proceeding with and now funding the iloperidone Phase III development program. All of our rights and economic interests in iloperidone, including royalties on sales of iloperidone, remain essentially unchanged under the agreement.

### **Spheramine and Other Cell Therapy Products**

In November 1992, we acquired an exclusive, worldwide license under certain U.S. and foreign patent applications relating to the CCM technology pursuant to a research and license agreement with New York University (NYU). The NYU agreement provides for the payment of royalties based on future net sales of products and processes incorporating the licensed technology, as well as a percentage of any income we receive from any sublicense thereof. We are also obligated to reimburse NYU for all costs and expenses incurred by NYU in filing, prosecuting and maintaining the licensed patents and patent applications. We must satisfy certain other terms and conditions of the NYU agreement in order to retain our license rights. These include, but are not limited to, the use of best efforts to bring licensed products to market as soon as commercially practicable and to diligently commercialize such products thereafter.

In January 2000, we entered into a sublicense agreement with Bayer Schering granting Bayer Schering exclusive worldwide commercialization rights to Spheramine. Under the agreement, we will collaborate with Bayer Schering on manufacturing and clinical development of cell therapy for the treatment of Parkinson's disease. We will receive funding for development activities, as well as potential reimbursement of certain prior research and development expenses. Bayer Schering will fully fund, and manage in collaboration with us, all future pilot and pivotal clinical studies, and manufacturing and development activities. Under the agreement, Bayer Schering will pay us a royalty on net sales of Spheramine.

### **DITPA**

In October 2003, through the acquisition of Developmental Therapeutics, Inc. (DTI), we acquired an exclusive worldwide license to an issued U.S. patent and pending international patent applications covering DITPA. Under this license agreement, we made an initial stock payment of 1,187,500 shares of our common stock and a cash payment of \$171,250 to the University of Arizona, the licensor of the technology, and will also make an additional payment of 712,500 shares of our common stock upon the achievement of positive pivotal study results or certain other substantial milestones within five years. A cash payment of \$102,750 or, alternatively, an additional payment of 37,500 shares of our common stock, will also be made to the licensor of the technology upon achievement of such study results or such other substantial milestones within five years. Also under this agreement, we are required to make royalty payments to the licensor based on net sales of products and processes incorporating the licensed technology, subject to minimum annual amounts commencing in the first year following the commercial sale of the product, as well as a percentage of any income derived from any sublicense of the licensed technology. In addition, we are required to make milestone payments to the licensor upon the achievement of certain clinical or regulatory milestones.

### **Gallium Complexes**

In August 2000, through the acquisition of GeoMed, Inc., we acquired an exclusive worldwide license to make, use and sell products developed under the patent rights to the compositions and application of gallium complexes. Under this license agreement, we are required to make an annual license payment to Dr. Lawrence Bernstein, technology inventor, of \$50,000, as well as royalty payments based on future net sales of products and processes incorporating the licensed technology. We must also pay all costs and expenses incurred in patent prosecution and maintenance.

In February 2004, we executed an agreement giving us an exclusive worldwide license to patent rights held by The Ohio State University covering the methods of treating arthritis using gallium compounds. Under this agreement, we are required to pay a license issuance fee and certain minimum annual royalty payments. In addition, we are required to pay royalties based on net sales of products and processes incorporating the licensed technology.

---

## [Index to Financial Statements](#)

In July 2005, we executed an agreement giving us an exclusive worldwide license to patent rights held by the University of Iowa Research Foundation covering the methods of treating biofilm formation, pseudomonas aeruginosa growth, human deficiency virus, and intracellular pathogens and pathogens causing chronic pulmonary infection using gallium maltolate. Under this agreement, we are required to pay a license issuance fee and certain minimum annual royalty payments. In addition, we are required to pay royalties based on net sales of products and processes incorporating the licensed technology.

In September 2006, we executed an agreement giving us an exclusive worldwide license to certain patent applications held by The MCW Research Foundation, Inc. covering the methods of treating cancer using novel gallium containing compounds in the field of human therapeutic treatment of lymphoma. Under this agreement, we are required to pay a one time license fee and royalties based on net sales of products and processes incorporating the licensed technology.

### **ProNeura Long-term Drug Delivery System**

In October 1995, we acquired from the Massachusetts Institute of Technology (MIT) an exclusive worldwide license to certain U.S. and foreign patents relating to the long-term drug delivery system. The exclusive nature of the MIT license is subject to certain conditions regarding timely performance of product development activities. We must also satisfy certain other usual terms and conditions set forth in the MIT license in order to retain our license rights, including payments of royalties based on sales of products and processes incorporating the licensed technology, as well as a percentage of income derived from sublicenses of the licensed technology.

### **Patents and Proprietary Rights**

We have obtained rights to certain patents and patent applications relating to our proposed products and may, in the future, seek rights from third parties to additional patents and patent applications. We also rely on trade secrets and proprietary know-how, which we seek to protect, in part, by confidentiality agreements with employees, consultants, advisors, and others. For risks we face with respect to patents and proprietary rights, see “Risk Factors—We may be unable to protect our patents and proprietary rights.”

### ***Iloperidone***

We hold a license from Sanofi-Aventis under one issued U.S. patent and certain foreign patents relating to iloperidone and its methods of use. Our license is exclusive for use in the treatment of psychiatric disorders, psychotic disorders and analgesia. The term of the U.S. patent that covers certain aspects of our iloperidone product expires in 2011. This does not include possible term extensions. Prosecution of various divisional and continuation applications and their foreign counterparts continues satisfactorily, although it is uncertain whether additional patents will be granted.

### ***Spheramine and Other Cell Therapy Products***

We are the exclusive licensee under a license agreement with NYU of certain U.S. and foreign patents and patent applications relating to our CCM technology. The U.S. Patent and Trademark Office has issued four U.S. patents on the core subject matter underlying the NYU license and an additional two patents relating to uses in delivery of gene therapy to the central nervous system. Prosecution of various foreign counterparts continues satisfactorily, although it is uncertain whether additional patents will be granted.

Patents have issued that cover certain aspects of our Spheramine product and its use, including four U.S. patents with patent terms expiring in 2010, 2014, 2015 and 2017, and one European patent, which has been unbundled as 15 national patents in various European countries, one Australian, two Japanese, one Hong Kong and one Canadian patent, all of which have patent terms expiring in 2011. Patents have issued relating to aspects of our gene transfer technology, including two U.S. patents with patent terms expiring in 2016, one European patent, one Canadian patent, two Australian patents, one South African patent, and one Taiwanese patent, all of which have patent terms expiring in 2017, and one Philippine patent with a patent term expiring in 2019. These dates do not include possible term extensions.

We are the owners of certain U.S. and foreign patents and patent applications relating to our CCM technology. Prosecution of patent applications relating to these technologies continues satisfactorily, as does prosecution of their foreign counterparts, although it is uncertain whether additional patents will be granted. Three foreign patents have issued that cover certain aspects of the use of our Spheramine product and other CCM technology, including one Australian and one New Zealand patent, both of which have patent terms expiring in 2018. We also are the owners of certain U.S. and foreign patents and patent applications relating to the application of our CCM technology to treat schizophrenia, including one U.S. patent, which has a patent term expiring in 2019, and one European patent, one New Zealand patent, one Australian patent, and one South African patent, which have patent terms expiring in 2020. These dates do not include possible term extensions.



### ***DITPA***

Through our wholly-owned subsidiary, Developmental Therapeutics, Inc., we hold an exclusive license from the University of Arizona to two issued U.S. patents with patent terms expiring in 2021, one pending U.S. patent application, one issued Mexican patent with a term expiring in 2022, and related pending foreign patent applications relating to the use of 3,5-diiodothyropropionic acid (DITPA) and other compounds for the treatment of heart failure in humans and for treatment of elevated cholesterol in a patient. These dates do not include possible term extensions.

### ***Gallium Complexes***

We are the exclusive licensee under the license agreement with Dr. Lawrence Bernstein of certain U.S. and foreign patents and patent applications relating to gallium complexes. 10 U.S. patents and several foreign patents have issued that cover pharmaceutical compositions and methods of use for gallium complexes. Prosecution of other foreign patent applications relating to this technology continues satisfactorily, although it is uncertain whether additional patents will be granted. U.S. patents in these families have patent terms expiring in 2009, 2010, and 2016. Foreign patents in these families have terms expiring in 2011 and 2017. These dates do not include possible term extensions. We are also the exclusive licensee under a license agreement with Ohio State University of certain issued U.S. and foreign patents related to the use of gallium compounds to treat rheumatoid arthritis. The U.S. patent term expires in 2009. In addition, we are licensees of certain issued U.S. and foreign patents and patent applications licensed from the University of Iowa, relating to methods of use to inhibit the growth of *P. aeruginosa*, and to treat infections caused by intracellular pathogens and pathogens causing chronic pulmonary infections, and human immunodeficiency virus infections. The two issued U.S. patents have terms expiring in 2019. We have also filed additional patent applications covering the use of gallium complexes in treating infection by intracellular prokaryotes, DNA viruses, and retroviruses, treating inflammatory arthritis, treatment and prevention of adverse liver conditions, and treatment of biofilm-associated infections. One issued Australian patent and one issued European patent, unbundled as seven national patents, relating to treating infection by intracellular prokaryotes, DNA viruses, and retroviruses, have terms expiring in 2021. These dates do not include possible term extensions. We are also the exclusive licensee under a license agreement with The MCW Research Foundation, Inc. of a U.S. patent application relating to the treatment of cancer using novel gallium containing compounds.

### ***ProNeura Long-term Drug Delivery System***

We are the exclusive licensee under the MIT license to three U.S. patents relating to a long-term drug delivery system, with patent terms expiring in 2007 and 2009, and certain European patents with patent terms expiring in 2008 and 2010. These dates do not include possible term extensions. Four additional patent applications have been filed which incorporate the use of specific compounds with the ProNeura technology, including two applications related to Probuphine.

### **Competition**

The pharmaceutical and biotechnology industries are characterized by rapidly evolving technology and intense competition. Many companies of all sizes, including major pharmaceutical companies and specialized biotechnology companies, are engaged in the development and commercialization of therapeutic agents designed for the treatment of the same diseases and disorders that we target. Many of our competitors have substantially greater financial and other resources, larger research and development staffs and more experience in the regulatory approval process. Moreover, potential competitors have or may have patents or other rights that conflict with patents covering our technologies.

### ***Probuphine***

Reckitt & Benckiser, Inc. received FDA approval in 2002 for a sublingual buprenorphine product for the treatment of opioid dependence. This product, to be administered daily, might compete with our six-month implantable product for opioid dependence. The FDA previously approved Orphan Drug designation, expiring in 2009, for Reckitt Benckiser's sublingual buprenorphine for the treatment of opioid dependence. Other forms of buprenorphine are also in development by other companies, including intramuscular injections and intranasally delivered buprenorphine, which also might compete with our product.

### ***lloperidone***

Several products categorized as atypical antipsychotics are already on the market. These products include Risperdal sold by Janssen Pharmaceuticals, Zyprexa sold by Eli Lilly, Clozaril sold by Novartis, Seroquel sold by AstraZeneca, Geodon sold by Pfizer, and Abilify sold by Bristol-Myers Squibb. Competition among these companies is already intense and

---

## [Index to Financial Statements](#)

iloperidone will face significant competition. The success of iloperidone will depend on how it can be differentiated from products already on the market on the basis of efficacy, side-effect profile, cost, availability of formulations and dose requirements, among other things.

### *Spheramine*

Several new treatments for Parkinson's disease are in pre-clinical and clinical development. In addition, several public and private companies, including StemCells, Inc., are actively pursuing alternative cell transplant technologies. Deep brain stimulation, also known as subthalamic stimulation is also a competing therapy for patients with advanced Parkinson's disease. The FDA has approved a stimulator device (Activa) manufactured by Medtronic, Inc., which is marketed in the U.S. We believe Spheramine may have potential competitive advantages to this therapy.

### *DITPA*

Several other companies are currently marketing drugs such as beta blockers, ace inhibitors and inotropes, which may be used for the treatment of heart failure. These companies include Abbott, AstraZeneca, Sanofi-Aventis, Johnson & Johnson, Pfizer and Sanofi-Synthelabo. In addition, companies such as Bristol-Myers Squibb, Merck and OSI Pharmaceuticals are developing new drugs which may be used to treat heart failure. Although DITPA represents a potential new class of agents for the treatment of CHF, these products may compete with DITPA.

Statins, alone or in combination, form the mainstay of therapy of hyperlipidemia. Several large pharmaceutical companies such as Pfizer, Merck, AstraZeneca, Schering Plough and Bristol-Myers Squibb currently market statins. Next generations of statins are also under development by companies such as Novartis and Bristol-Myers Squibb. In addition, several smaller companies (e.g. Metabasis Therapeutics, Forbes Medi Tech and Avant Immunotherapeutics) are also attempting to develop novel therapeutics for this indication.

### *Gallium Complexes*

Intravenously administered gallium nitrate is approved to treat hypercalcemia related to malignancy and may have potential for treatment of certain cancers. Other intravenous products, including the bisphosphonates, are available or are in development in the U.S. or Europe to treat osteoporosis, Paget's disease, primary hyperparathyroidism, hypercalcemia of malignancy and metastatic bone disease. Our product, gallium maltolate, is an orally administered drug and may have potential advantages in the treatment of cancer as well as bone-related diseases. Genta has previously stated that it is developing oral gallium compounds to treat bone-losing conditions.

See "Risk Factors—We face intense competition."

### **Manufacturing**

We utilize contract manufacturing organizations to manufacture our products for pre-clinical studies and clinical trials. While we have not introduced any products on the commercial market to date, at such time as we are ready to do so we will need to allocate additional resources to the manufacture of these products. We do not have the facilities to manufacture these products in-house nor do we intend to establish our own manufacturing operation at this time. We currently plan to pursue collaborative arrangements regarding the manufacture of any products that we may successfully develop.

### **Government Regulation**

In order to obtain FDA approval of a new drug, a company generally must submit proof of purity, potency, safety and efficacy, among other regulatory standards. In most cases, such proof entails extensive clinical and pre-clinical laboratory tests.

The procedure for obtaining FDA approval to market a new drug involves several steps. Initially, the manufacturer must conduct pre-clinical animal testing to demonstrate that the product does not pose an unreasonable risk to human subjects in clinical studies. Upon completion of such animal testing, an Investigational New Drug application, or IND, must be filed with the FDA before clinical studies may begin. An IND application consists of, among other things, information about the proposed clinical trials. Among the conditions for clinical studies and IND approval is the requirement that the prospective manufacturer's quality control and manufacturing procedures conform to current Good Manufacturing Practices (cGMP), which must be followed at all times. Once the IND is approved (or if the FDA does not respond within 30 days), the clinical trials may begin.

Human clinical trials on drugs are typically conducted in three sequential phases, although the phases may overlap. Phase I trials typically consist of testing the product in a small number of healthy volunteers or patients, primarily for safety

---

## [Index to Financial Statements](#)

in one or more doses. During Phase II, in addition to safety, dose selection and efficacy of the product is evaluated in up to several hundred patients and sometimes more. Phase III trials typically involve additional testing for safety and confirmation of efficacy in an expanded patient population at multiple test sites. The FDA may order the temporary or permanent discontinuation of a clinical trial at any time.

The results of the pre-clinical and clinical testing on new drugs, if successful, are submitted to the FDA in the form of a New Drug Application, or NDA. The NDA approval process requires substantial time and effort and there can be no assurance that any approval will be granted on a timely basis, if at all. The FDA may refuse to approve an NDA if applicable regulatory requirements are not satisfied. Product approvals, if granted, may be withdrawn if compliance with regulatory standards is not maintained or problems occur following initial marketing.

The FDA may also require post-marketing testing and surveillance of approved products, or place other conditions on their approvals. These requirements could cause it to be more difficult or expensive to sell the products, and could therefore restrict the commercial applications of such products. Product approvals may be withdrawn if compliance with regulatory standards is not maintained or if problems occur following initial marketing. With respect to patented products or technologies, delays imposed by the governmental approval process may materially reduce the period during which we will have the exclusive right to exploit such technologies.

We believe we are in compliance with all material applicable regulatory requirements. However, see “Risk Factors—We must comply with extensive government regulations” for additional risks we face regarding regulatory requirements and compliance.

### **Foreign Regulatory Issues**

Sales of pharmaceutical products outside the United States are subject to foreign regulatory requirements that vary widely from country to country. Whether or not FDA approval has been obtained, approval of a product by a comparable regulatory authority of a foreign country must generally be obtained prior to the commencement of marketing in that country. Although the time required to obtain such approval may be longer or shorter than that required for FDA approval, the requirements for FDA approval are among the most detailed in the world and FDA approval generally takes longer than foreign regulatory approvals.

### **Employees**

At December 31, 2006 we had 38 full-time employees. None of our employees are represented by a labor union. We have not experienced any work stoppages and consider our relations with our employees to be good. See “Risk Factors—We may not be able to retain our key management and scientific personnel.”

### **Available Information**

We electronically file our annual reports on Form 10-K, quarterly reports on Form 10-Q and current reports on Form 8-K with the Securities and Exchange Commission (SEC) pursuant to Section 13(a) or 15(d) of the Securities Exchange Act of 1934. Any materials we file with the SEC are accessible to the public at the SEC’s Public Reference Room at 450 Fifth Street, NW, Washington, DC 20549. You may obtain information on the operation of the SEC’s Public Reference Room by calling the SEC at (800) SEC-0330. The public may also utilize the SEC’s Internet website, which contains reports, proxy and information statements, and other information regarding issuers that file electronically with the SEC. The address of the SEC website is <http://www.sec.gov>.

You may obtain free copies of our annual reports on Form 10-K, quarterly reports on Form 10-Q and current reports on Form 8-K and amendments to those reports on our website at <http://www.titanpharm.com>, or by contacting our corporate office by calling (650) 244-4990, or by sending an e-mail message to [info@titanpharm.com](mailto:info@titanpharm.com).

**Item 1A. Risk Factors**

Our business is subject to numerous risks.

**We have a history of operating losses and may never be profitable.**

From our inception through December 31, 2006, we had an accumulated deficit of approximately \$223.9 million. We will continue to incur losses for the foreseeable future as a result of the various costs associated with our research, development, financial, administrative, regulatory and management activities. We may never achieve or sustain profitability.

**Our products are at various stages of development and may not be successfully developed or commercialized.**

We do not currently have any products being sold on the commercial market. Our proposed products are at various stages of development, but all will require significant further capital expenditures, development, testing, and regulatory clearances prior to commercialization. Of the large number of drugs in development, only a small percentage successfully complete the U.S. Food and Drug Administration (FDA) regulatory approval process and are commercialized. We are subject to the risk that some or all of our proposed products:

- will be found to be ineffective or unsafe;
- will not receive necessary regulatory clearances;
- will be unable to get to market in a timely manner;
- will not be capable of being produced in commercial quantities at reasonable costs;
- will not be successfully marketed; or
- will not be widely accepted by the physician community.

To date, we have experienced setbacks in some of our product development efforts. For example, the results of a study evaluating the EKG profile of patients taking iloperidone lead to a significant delay in the development of that product, a vaccine product formerly under development failed to meet the study's primary endpoint, and a study of one of our products in a combination treatment was discontinued as a result of an interim safety analysis.

In addition, our Spheramine product is based upon new technology which may be risky and fail to show efficacy. We are not aware of any other cell therapy products for CNS disorders that have been approved by the FDA or any similar foreign government entity and cannot assure you that we will be able to obtain the required regulatory approvals for any products based upon such technology.

We may continue to experience unanticipated problems relating to product development, testing, regulatory compliance, manufacturing, marketing and competition, and our costs and expenses could exceed current estimates. We cannot predict whether we will successfully develop and commercialize any products.

**We must comply with extensive government regulations.**

Our research, development, preclinical and clinical trial activities and the manufacture and marketing of any products that we may successfully develop are subject to an extensive regulatory approval process by the FDA and other regulatory agencies in the U.S. and other countries. The process of obtaining required regulatory approvals for drugs, including conducting preclinical and clinical testing to determine safety and efficacy, is lengthy, expensive and uncertain. Even after such time and expenditures, we may not obtain necessary regulatory approvals for clinical testing or for the manufacturing or marketing of any products. We have limited experience in obtaining FDA approval. Regulatory approval may entail limitations on the indicated usage of a drug, which may reduce the drug's market potential. Even if regulatory clearance is obtained, post-market evaluation of the products, if required, could result in restrictions on a product's marketing or withdrawal of the product from the market, as well as possible civil and criminal sanctions. Our regulatory submissions may be delayed or we may cancel plans to make submissions for proposed products for a number of reasons, including:

- unanticipated preclinical testing or clinical trial reports;
- failure to reach agreement with the FDA regarding study protocols or endpoints;
- changes in regulations or the adoption of new regulations;
- unanticipated enforcement of existing regulations;
- unexpected technological developments; and
- developments by our competitors.

---

## [Index to Financial Statements](#)

For example, we have initiated a Phase III clinical study while we continue to have discussions with the FDA relating to finalizing the Probuphine development program. If our corporate partners and we are unable to obtain regulatory approval for our products, our business will be seriously harmed.

In addition, we and our collaborative partners may be subject to regulation under state and federal laws, including requirements regarding occupational safety, laboratory practices, environmental protection and hazardous substance control, and may be subject to other local, state, federal and foreign regulation. We cannot predict the impact of such regulation on us, although it could seriously harm our business.

### **We face risks associated with third parties conducting preclinical studies and clinical trials of our products as well as our dependence on third parties to manufacture any products that we may successfully develop.**

We depend on third-party laboratories and medical institutions to conduct preclinical studies and clinical trials for our products and other third-party organizations to perform data collection and analysis, all of which must maintain both good laboratory and good clinical practices. We will also depend upon third party manufacturers for the production of any products we may successfully develop to comply with current Good Manufacturing Practices of the FDA, which are similarly outside our direct control. If third party laboratories and medical institutions conducting studies of our products fail to maintain both good laboratory and clinical practices, the studies could be delayed or have to be repeated. Similarly, if the manufacturers of any products we develop in the future fail to comply with current Good Manufacturing Practices of the FDA, we may be forced to cease manufacturing such product until we have found another third party to manufacture the product.

### **We face many uncertainties relating to our human clinical trial strategy and results.**

In order to obtain the regulatory approvals that we need to commercialize any of our product candidates, we must demonstrate that each product candidate is safe and effective for use in humans for each target indication. The results of preclinical and Phase I and Phase II clinical studies are not necessarily indicative of whether a product will demonstrate safety and efficacy in large patient populations. Although two of our product candidates have reached Phase III human clinical trials, results from the studies have not supported a regulatory filing. Several other product candidates are currently advancing into Phase II human clinical trials. We may not be able to demonstrate that any of our product candidates will be safe or effective in advanced trials that involve larger numbers of patients. Clinical trials are subject to oversight by institutional review boards and the FDA and:

- must be conducted in conformance with the FDA's good laboratory practice regulations;
- must meet requirements for institutional review board oversight;
- must meet requirements for informed consent;
- must meet requirements for good clinical practices;
- are subject to continuing FDA oversight; and
- may require large numbers of test subjects.

As described above in "Our products are at various stages of development and may not be successfully developed or commercialized," our product development programs have in the past been and may in the future be curtailed, redirected or eliminated at any time for some or all of the following reasons:

- unanticipated, negative or ambiguous results;
- undesirable side effects which delay or extend the trials;
- our inability to locate, recruit and qualify a sufficient number of patients for our trials;
- regulatory delays or other regulatory actions;
- difficulties in manufacturing sufficient quantities of the particular product candidate or any other components needed for our preclinical testing or clinical trials;
- change in the focus of our development efforts; and
- reevaluation of our clinical development strategy.

Accordingly, our clinical trials may not proceed as anticipated or otherwise adequately support our applications for regulatory approval.

**We face risks associated with clinical trial liability claims in the event that the use or misuse of our product candidates results in personal injury or death.**

We face an inherent risk of clinical trial liability claims in the event that the use or misuse of our product candidates results in personal injury or death. Our clinical liability insurance coverage may not be sufficient to cover claims that may be made against us. Any claims against us, regardless of their merit, could severely harm our financial condition, strain our management and other resources or destroy the prospects for commercialization of the product which is the subject of any such claim.

**We may be unable to protect our patents and proprietary rights.**

Our future success will depend to a significant extent on our ability to:

- obtain and keep patent protection for our products and technologies on an international basis;
- enforce our patents to prevent others from using our inventions;
- maintain and prevent others from using our trade secrets; and
- operate and commercialize products without infringing on the patents or proprietary rights of others.

We cannot assure you that our patent rights will afford any competitive advantages, and these rights may be challenged or circumvented by third parties. Further, patents may not be issued on any of our pending patent applications in the U.S. or abroad. Because of the extensive time required for development, testing and regulatory review of a potential product, it is possible that before a potential product can be commercialized, any related patent may expire or remain in existence for only a short period following commercialization, reducing or eliminating any advantage of the patent. If we sue others for infringing our patents, a court may determine that such patents are invalid or unenforceable. Even if the validity of our patent rights is upheld by a court, a court may not prevent the alleged infringement of our patent rights on the grounds that such activity is not covered by our patent claims.

In addition, third parties may sue us for infringing their patents. In the event of a successful claim of infringement against us, we may be required to:

- pay substantial damages;
- stop using our technologies and methods;
- stop certain research and development efforts;
- develop non-infringing products or methods; and
- obtain one or more licenses from third parties.

If required, we cannot assure you that we will be able to obtain such licenses on acceptable terms, or at all. If we are sued for infringement, we could encounter substantial delays in development, manufacture and commercialization of our product candidates. Any litigation, whether to enforce our patent rights or to defend against allegations that we infringe third party rights, will be costly, time consuming, and may distract management from other important tasks.

As is commonplace in the biotechnology and pharmaceutical industry, we employ individuals who were previously employed at other biotechnology or pharmaceutical companies, including our competitors or potential competitors. To the extent our employees are involved in research areas which are similar to those areas in which they were involved at their former employers, we may be subject to claims that such employees and/or we have inadvertently or otherwise used or disclosed the alleged trade secrets or other proprietary information of the former employers. Litigation may be necessary to defend against such claims, which could result in substantial costs and be a distraction to management even if we are successful in defending such claims.

We also rely in our business on trade secrets, know-how and other proprietary information. We seek to protect this information, in part, through the use of confidentiality agreements with employees, consultants, advisors and others. Nonetheless, we cannot assure you that those agreements will provide adequate protection for our trade secrets, know-how or other proprietary information and prevent their unauthorized use or disclosure. To the extent that consultants, key employees or other third parties apply technological information independently developed by them or by others to our proposed products, disputes may arise as to the proprietary rights to such information, which may not be resolved in our favor. Most of our consultants are employed by, or have consulting agreements with, third parties and any inventions discovered by such individuals generally will not become our property. There is a risk that other parties may breach confidentiality agreements or that our trade secrets may become known or independently discovered by competitors.

**We face intense competition.**

Competition in the pharmaceutical and biotechnology industries is intense. We face, and will continue to face, competition from numerous companies that currently market, or are developing, products for the treatment of the diseases and disorders we have targeted. Many of these entities have significantly greater research and development capabilities, experience in obtaining regulatory approvals and manufacturing, marketing, financial and managerial resources than we have. We also compete with universities and other research institutions in the development of products, technologies and processes, as well as the recruitment of highly qualified personnel. Our competitors may succeed in developing technologies or products that are more effective than the ones we have under development or that render our proposed products or technologies noncompetitive or obsolete. In addition, our competitors may achieve product commercialization or patent protection earlier than we will.

**We are dependent upon our key collaborative relationships and license and sponsored research agreements.**

As a company with limited resources, we rely significantly on the resources of third parties to conduct research and development and complete the regulatory approval process on our behalf. For example, our ability to ultimately derive revenues from iloperidone is almost entirely dependent upon Novartis and Vanda Pharmaceuticals conducting the Phase III trials and completing the regulatory approval process and implementing the marketing program necessary to commercialize iloperidone if the product is approved by the FDA. We are similarly dependent upon Bayer Schering, our collaborator for the development and commercialization of Spheramine. Beyond our contractual rights, we cannot control the amount or timing of resources that any existing or future corporate partner devotes to product development and commercialization efforts for our product candidates. In addition, we also receive substantial government funding for our cancer immunotherapeutic programs. We cannot assure you that we will continue to receive such governmental funding. If such funds are no longer available, some of our current and future development efforts may be delayed or terminated. We depend on our ability to maintain existing collaborative relationships, to develop new collaborative relationships with third parties and to acquire or in-license additional products and technologies for the development of new product candidates. We cannot assure you that we will be able to maintain or develop new collaborative relationships, or that any such third-party products or technology will be available on acceptable terms, if at all.

Conflicts with our collaborators and strategic partners could result in strained relationships with them and impair our ability to enter into future collaborations, either of which could seriously harm our business. Our collaborators have, and may, to the extent permitted by our agreements, develop competing products, preclude us from entering into collaborations with their competitors or terminate their agreements with us prematurely. Moreover, disagreements could arise with our collaborators or strategic partners over rights to our intellectual property and our rights to share in any of the future revenues from products or technologies resulting from use of our technologies, or our activities in separate fields may conflict with other business plans of our collaborators.

**We must meet payment and other obligations under our license and sponsored research agreements.**

Our license agreements relating to the in-licensing of technology generally require the payment of up-front license fees and royalties based on sales with minimum annual royalties, the use of due diligence in developing and bringing products to market, the achievement of funding milestones and, in some cases, the grant of stock to the licensor. Our sponsored research agreements generally require periodic payments on an annual or quarterly basis. Our failure to meet financial or other obligations under license or sponsored research agreements in a timely manner could result in the loss of our rights to proprietary technology or our right to have the applicable university or institution conduct research and development efforts.

**We may be dependent upon third parties to manufacture and market any products we successfully develop.**

We currently do not have the resources or capacity to commercially manufacture or directly market any of our proposed products. Collaborative arrangements may be pursued regarding the manufacture and marketing of any products that may be successfully developed. We may be unable to enter into additional collaborative arrangements to manufacture or market any proposed products or, in lieu thereof, establish our own manufacturing operations or sales force.

**Healthcare reform and restrictions on reimbursements may limit our financial returns.**

Our ability or the ability of our collaborators to commercialize drug products, if any, may depend in part on the extent to which government health administration authorities, private health insurers and other organizations will reimburse consumers for the cost of these products. These third parties are increasingly challenging both the need for and the price of new drug products. Significant uncertainty exists as to the reimbursement status of newly approved therapeutics. Adequate third party reimbursement may not be available for our own or our collaborator's drug products to enable us or them to maintain price levels sufficient to realize an appropriate return on their and our investments in research and product development.

**We may not be able to retain our key management and scientific personnel.**

As a company with a limited number of personnel, we are highly dependent on the services of Dr. Louis R. Bucalo, our Chairman, President and Chief Executive Officer, as well as the other principal members of our management and scientific staff. The loss of one or more of such individuals could substantially impair ongoing research and development programs and could hinder our ability to obtain corporate partners. Our success depends in large part upon our ability to attract and retain highly qualified personnel. We compete in our hiring efforts with other pharmaceutical and biotechnology companies, as well as universities and nonprofit research organizations, and we may have to pay higher salaries to attract and retain personnel.

**We will need additional financing.**

At December 31, 2006, we had approximately \$13.7 million of cash, cash equivalents, and marketable securities. Our financing agreement with Cornell Capital Partners can provide us with up to an additional \$31.0 million, subject to shareholder approval for certain amounts under this agreement. We will need to seek additional financing to continue our product development activities, and will be required to obtain substantial funding to commercialize any products other than iloperidone or Spheramine that we may successfully develop. Other than the Standby Equity Distribution Agreement with Cornell Capital Partners, we do not have any funding commitments or arrangements. If we are unable to generate adequate revenues, enter into a corporate collaboration, complete a debt or equity offering, or otherwise obtain sufficient financing when and if needed, we may be required to reduce, defer or discontinue one or more of our product development programs.

**Future sales of our common stock in the public market could adversely impact our stock price.**

Future sales of our common stock by existing stockholders pursuant to Rule 144 under the Securities Act, pursuant to an effective registration statement or otherwise, could decrease the price of our common stock.

**Our stock price has been and will likely continue to be volatile.**

Our stock price has experienced substantial fluctuations and could continue to fluctuate significantly due to a number of factors, including:

- variations in our anticipated or actual operating results;
- sales of substantial amounts of our common stock;
- announcements about us or about our competitors, including introductions of new products;
- litigation and other developments relating to our patents or other proprietary rights or those of our competitors;
- conditions in the pharmaceutical or biotechnology industries;
- governmental regulation and legislation; and
- change in securities analysts' estimates of our performance, or our failure to meet analysts' expectations.

**The market price of our common stock may fluctuate in a way that is disproportionate to our operating performance.**

The stock markets in general, and the American Stock Exchange and the market for pharmaceutical and biotechnological companies in particular, have experienced extreme price and volume fluctuations recently. These fluctuations often have been unrelated or disproportionate to the operating performance of these companies. These broad market and industry factors could reduce the market price of our common stock, regardless of our actual operating performance.

**Cornell Capital Partners may sell shares of our common stock after we deliver a draw-down notice during the pricing period, which could cause our stock price to decline.**

Cornell Capital Partners is deemed to beneficially own the shares of common stock corresponding to a particular draw-down on the date that we deliver a draw-down notice to Cornell Capital Partners, which is prior to the date the stock is delivered to Cornell Capital Partners. Cornell Capital Partners may sell such shares any time after we deliver a draw-down notice. Accordingly, Cornell Capital Partners may sell such shares during the pricing period. Such sales may cause our stock price to decline and if so would result in a lower volume weighted average price during the pricing period, which would result in us having to issue a larger number of shares of common stock to Cornell Capital Partners in respect of the draw-down.



---

## [Index to Financial Statements](#)

### **Sales of our shares of common stock under the Standby Equity Distribution Agreement could result in significant dilution to the existing shareholders.**

The issuance of shares of our common stock under the Standby Equity Distribution Agreement will dilute our existing stockholders and the issuance or even potential issuance of such shares could have a negative effect on the market price of our common stock. As a result, our net income per share could decrease in future periods, and the market price of our common stock could decline. In addition, the lower our stock price, the more shares of common stock we will have to issue under the Standby Equity Distribution Agreement to draw-down the full amount. If our stock price is lower, then our existing stockholders would experience greater dilution.

### **Sales of our stock under the Standby Equity Distribution Agreement could encourage short sales by third parties which could contribute to the future decline of our stock price.**

The provisions of the Standby Equity Distribution Agreement have the potential to cause downward pressure on the price of our common stock, if the shares being placed into the market exceed the market's current ability to buy the stock. Such an event could place downward pressure on the price of our common stock. We may request numerous draw-downs pursuant to the terms of the Standby Equity Distribution Agreement.

### **We may not be able to make a draw-down under the Standby Equity Distribution Agreement if Cornell Capital Partners holds more than 9.9% of our common stock.**

Pursuant to our agreement with Cornell Capital Partners, in the event Cornell Capital Partners holds more than 9.9% of our then-outstanding common stock, we will be unable to make a draw-down under the Standby Equity Distribution Agreement. A possibility exists that Cornell Capital Partners may own more than 9.9% of our outstanding common stock at a time when we would otherwise plan to make a draw-down under the Standby Equity Distribution Agreement. In that event, if we are unable to obtain additional external funding, we could be forced to curtail or cease our operations.

### **We will not be able to make a draw-down under the Standby Equity Distribution Agreement if we would be required to issue more than 6,475,287 shares of our common stock unless we obtain stockholder approval for such issuance.**

Under American Stock Exchange rules, we will not be able to issue more than 6,475,287 shares of our common stock in the aggregate to Cornell Capital Partners pursuant to the Standby Equity Distribution Agreement unless we obtain stockholder approval prior to the issuance of such greater number of shares. If we want to make a draw-down under the Standby Equity Distribution Agreement but have already issued the maximum number of shares and are unable to obtain stockholder approval for such issuance in a timely fashion, we will be forced to seek an alternate financing source. There can be no guarantee that alternative sources may be available. To date, we have issued 3,131,228 shares, including 80,793 shares related to commitment and structuring fees, and can only issue 3,344,059 additional shares without receipt of the required shareholder approval.

### **Item 1B. Unresolved Staff Comments**

None.

### **Item 2. Properties**

We have a five-year operating lease, expiring in June 2010, for approximately 22,595 square feet of office space in South San Francisco, California. We also have a one-year lease, expiring in December 2007, for approximately 2,100 square feet of office and laboratory space in Somerville, New Jersey.

### **Item 3. Legal Proceedings**

In March 2005, Dr. Bernard Sabel initiated an appraisal proceeding in the Court of Chancery of the State of Delaware relating to the merger of Titan's subsidiary ProNeura, Inc. into Titan. The complaint indicates that Mr. Sabel wants the court to appraise the value of the 108,800 shares of the common stock of ProNeura owned by him. The complaint does not specify an amount that Mr. Sabel considers the fair value of the shares. Discovery is proceeding in connection with this appraisal proceeding.

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

None.

**PART II**

**Item 5. Market for Registrant's Common Equity and Related Stockholder Matters.**

**(a) Price Range of Securities**

Our common stock trades on the American Stock Exchange under the symbol TTP. The table below sets forth the high and low sales prices of our common stock as reported by the American Stock Exchange for the periods indicated.

	<u>High</u>	<u>Low</u>
Fiscal Year Ended December 31, 2006:		
First Quarter	\$4.99	\$1.35
Second Quarter	\$3.39	\$1.69
Third Quarter	\$2.52	\$1.65
Fourth Quarter	\$4.10	\$1.92
Fiscal Year Ended December 31, 2005:		
First Quarter	\$3.24	\$2.20
Second Quarter	\$2.47	\$1.80
Third Quarter	\$2.31	\$1.73
Fourth Quarter	\$1.89	\$1.19

**(b) Approximate Number of Equity Security Holders**

The number of record holders of our common stock as of March 1, 2007 was approximately 136. Based on the last ADP search, we believe there are in excess of 10,000 beneficial holders of our common stock.

**(c) Dividends**

We have never paid a cash dividend on our common stock and anticipate that for the foreseeable future any earnings will be retained for use in our business and, accordingly, do not anticipate the payment of cash dividends.

## [Index to Financial Statements](#)

### Item 6. Selected Financial Data

The selected financial data presented below summarizes certain financial data which has been derived from and should be read in conjunction with our consolidated financial statements and notes thereto included in the section beginning on page F-1. See also "Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations."

	Years Ended December 31,				
	2006	2005	2004	2003	2002
	(in thousands, except per share data)				
<b>Statement of Operations Data:</b>					
Total revenue(1)	\$ 32	\$ 89	\$ 31	\$ 89	\$ 2,892
Operating expenses:					
Research and development	11,620	17,770	20,415	22,258	29,819
Acquired/in-process research and development(2)	—	—	759	3,896	—
General and administrative	4,859	5,370	5,237	5,109	5,076
Other income, net	710	589	376	1,285	3,821
Net loss	<u>\$(15,737)</u>	<u>\$(22,462)</u>	<u>\$(26,004)</u>	<u>\$(29,889)</u>	<u>\$(28,182)</u>
Basic and diluted net loss per share	\$ (0.42)	\$ (0.69)	\$ (0.83)	\$ (1.07)	\$ (1.02)
Shares used in computing:					
Basic and diluted net loss per share	37,902	32,635	31,381	27,907	27,642

(1) Revenues for 2002 include a \$2.0 million milestone payment from Bayer Schering Pharma AG.

(2) Acquired research and development reflects the acquisition of the minority shares of ProNeura in 2004 and the acquisition of DTI in 2003.

	As of December 31,				
	2006	2005	2004	2003	2002
	(in thousands)				
<b>Balance Sheet Data:</b>					
Cash, cash equivalents, and marketable securities	\$13,715	\$17,369	\$36,322	\$46,555	\$73,450
Working capital	10,825	15,449	33,760	44,578	70,702
Total assets	15,040	19,737	38,626	49,008	75,926
Total stockholders' equity	10,405	15,360	33,713	44,426	70,740

## [Index to Financial Statements](#)

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

The following discussion should be read in conjunction with the Consolidated Financial Statements and Notes thereto beginning on page F-1 in this report.

The following discussion contains certain forward-looking statements, within the meaning of the “safe harbor” provisions of the Private Securities Reform Act of 1995, the attainment of which involves various risks and uncertainties. Forward-looking statements may be identified by the use of forward-looking terminology such as “may,” “will,” “expect,” “believe,” “estimate,” “plan,” “anticipate,” “continue,” or similar terms, variations of those terms or the negative of those terms. Our actual results may differ materially from those described in these forward-looking statements due to, among other factors, the results of ongoing research and development activities and pre-clinical testing, the results of clinical trials and the availability of additional financing through corporate partnering arrangements or otherwise.

Probuphine<sup>®</sup>, Spheramine<sup>®</sup>, ProNeura<sup>™</sup> and CCM<sup>™</sup> are trademarks of Titan Pharmaceuticals, Inc. This Form 10-K also includes trade names and trademarks of companies other than Titan Pharmaceuticals, Inc.

#### **Overview**

We are a biopharmaceutical company developing proprietary therapeutics for the treatment of central nervous system (CNS) disorders, cardiovascular disease, bone disease and other disorders. Our product development programs focus primarily on large pharmaceutical markets with significant unmet medical needs and commercial potential. We are focused primarily on clinical development of the following products:

- Probuphine: for the treatment of opioid dependence
- Iloperidone: for the treatment of schizophrenia and related psychotic disorders (partnered with Vanda Pharmaceuticals, Inc.)
- Spheramine: for the treatment of advanced Parkinson’s disease (partnered with Bayer Schering Pharma AG)
- DITPA: for the treatment of cardiovascular disease
- Gallium maltolate: for the treatment of bone related diseases, chronic bacterial infections and cancer

We are directly developing our product candidates and also utilizing corporate partnerships, including a collaboration with (i) Bayer Schering Pharma AG, Germany (Bayer Schering) for the development of Spheramine to treat Parkinson’s disease, and (ii) Vanda Pharmaceuticals, Inc. (Vanda) for the development of iloperidone for the treatment of schizophrenia and related psychotic disorders. We also utilize grants from government agencies to fund development of our product candidates.

The following table provides summary status of our products in development:

<b>Product</b>	<b>Potential Indication(s)</b>	<b>Phase of Development</b>	<b>Marketing Rights</b>
Probuphine	Opioid dependence	Phase III	Titan
Iloperidone	Schizophrenia, psychosis	Phase III	Vanda Pharmaceuticals, Inc.
Spheramine	Parkinson’s disease	Phase IIb	Bayer Schering Pharma AG
DITPA	Hyperlipidemia	Phase II	Titan
Gallium maltolate	Bone related disease, chronic bacterial infections, cancer	Phase I	Titan

---

## [Index to Financial Statements](#)

Our products are at various stages of development and may not be successfully developed or commercialized. We do not currently have any products being commercially sold. Our proposed products will require significant further capital expenditures, development, testing, and regulatory clearances prior to commercialization. We may experience unanticipated problems relating to product development and cannot predict whether we will successfully develop and commercialize any products. An estimation of product completion dates and completion costs can vary significantly for each product and are difficult to predict. Various statutes and regulations also influence our product development progress and the success of obtaining approval is highly uncertain. We will also continue to identify new technologies and/or product candidates for possible in-licensing or acquisition. Accordingly, we expect to incur operating losses for the foreseeable future. We cannot assure you that we will ever achieve profitable operations. For a full discussion of risks and uncertainties in our product development, see “Risk Factors—Our products are at various stages of development and may not be successfully developed or commercialized.”

### **Critical Accounting Policies and the Use of Estimates**

The preparation of our financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the amounts reported in our consolidated financial statements and accompanying notes. Actual results could differ materially from those estimates. We believe the following accounting policy for the year ended December 31, 2006, to be applicable:

In December 2004, the Financial Accounting Standards Board (FASB) issued their final standard on accounting for share-based payments in FASB Standard No. 123R (revised 2004), *Share-Based Payment* (SFAS 123R). This statement replaces FASB Statement 123, *Accounting for Stock-Based Compensation* (SFAS 123), and supersedes Accounting Principles Board (APB) Opinion No. 25, *Accounting for Stock Issued to Employees*. The statement is effective for all interim and annual periods beginning after December 15, 2005 and requires companies to measure and recognize compensation expense for all share-based payments at fair value in the consolidated statement of income.

Effective January 1, 2006, we adopted SFAS 123R using the modified-prospective-transition method. Under this transition method, stock compensation cost recognized beginning January 1, 2006 includes: (a) compensation cost for all share-based payments granted prior to, but not yet vested as of January 1, 2006, based on the grant-date fair value estimated in accordance with the original provisions of SFAS 123, and (b) compensation cost for all share-based payments granted on or subsequent to January 1, 2006, based on the grant-date fair value estimated in accordance with the provisions of SFAS 123R. Results for prior periods have not been restated.

### **Results of Operations**

#### *Comparison of Years Ended December 31, 2006 and 2005*

Revenues in 2006 were \$32,000 compared to \$89,000 for 2005, a decrease of \$57,000. Our revenues during 2006 and 2005 were derived from fees received under various licensing agreements.

Research and development expenses for 2006 were \$11.6 million compared to \$17.8 million for 2005, a decrease of \$6.2 million. The decrease in research and development was primarily associated with the conclusion of certain clinical study related activities and cost reduction strategies initiated in the third quarter of 2005 resulting in lower internal expenditures in

## Index to Financial Statements

2006. Of our 2006 research and development expenses, approximately 46%, or \$5.3 million, were attributable to external R&D expenses. External R&D expenses include direct expenses such as clinical research organization charges, investigator and review board fees, patient expense reimbursements, pre-clinical activities and contract manufacturing expenses. In 2006, approximately \$2.2 million of external R&D expenses were related to Probuphine, \$2.6 million to DITPA, \$0.4 million to gallium maltolate, and the remainder to other projects. Remaining R&D expenses were attributable to internal operating costs, which include clinical research and development personnel salaries and employment related expenses, clinical trials related travel expenses, and allocation of facility and corporate costs. In October 2006, we determined to focus our resources on the Phase III development of Probuphine, and have discontinued further enrollment in our Phase II study of DITPA in congestive heart failure (CHF). We will subsequently analyze data collected to date. In addition, the Department of Veteran's Affairs indicated that it will discontinue its Cooperative Studies Program Phase II study of DITPA in CHF patients.

As a result of the risks and uncertainties inherently associated with pharmaceutical research and development activities described elsewhere in this report, we are unable to estimate the specific timing and future costs of our clinical development programs or the timing of material cash inflows, if any, from our product candidates.

General and administrative expenses for 2006 were \$4.9 million compared to \$5.4 million for 2005, a decrease of \$0.5 million.

Other income, net, for 2006 was \$710,000 compared to \$589,000 for 2005, an increase of \$121,000.

As a result of the foregoing, we had a net loss of \$15.8 million in 2006 compared to a net loss of \$22.5 million in 2005.

### ***Comparison of Years Ended December 31, 2005 and 2004***

Revenues in 2005 were \$89,000 compared to \$31,000 for 2004, an increase of \$58,000. Our revenues during 2005 and 2004 were derived from fees received under various licensing agreements.

Research and development expenses for 2005 were \$17.8 million compared to \$20.4 million for 2004, a decrease of \$2.6 million. The decrease in research and development was primarily associated with the conclusion of certain clinical studies in 2004 and cost reduction strategies initiated in 2005 resulting in lower internal expenditures in 2005. Of our 2005 research and development expenses, approximately 38%, or \$6.8 million, were attributable to external R&D expenses. External R&D expenses include direct expenses such as clinical research organization charges, investigator and review board fees, patient expense reimbursements, pre-clinical activities and contract manufacturing expenses. In 2005, approximately \$2.4 million of external R&D expenses were related to Probuphine, \$2.7 million to DITPA, \$0.7 million to gallium maltolate, and the remainder to other projects. Remaining R&D expenses were attributable to internal operating costs, which include clinical research and development personnel salaries and employment related expenses, clinical trials related travel expenses, and allocation of facility and corporate costs. In 2004, we recorded a \$759,000 acquired research and development expense in connection with the acquisition of minority shares of ProNeura, Inc. The entire purchase price of the shares was charged to acquired research and development on the acquisition date in accordance with generally accepted accounting principles.

General and administrative expenses for 2005 were \$5.4 million compared to \$5.2 million for 2004.

Other income, net, for 2005 was \$589,000 compared to \$376,000 for 2004, an increase of \$213,000.

As a result of the foregoing, we had a net loss of \$22.5 million in 2005 compared to a net loss of \$26.0 million in 2004.

## **Liquidity and Capital Resources**

	<u>2006</u>	<u>2005</u>	<u>2004</u>
	(in thousands)		
<b>As of December 31:</b>			
Cash, cash equivalents and marketable securities	\$ 13,715	\$ 17,369	\$ 36,322
Working capital	\$ 10,825	\$ 15,449	\$ 33,760
Current ratio	4.2:1	5.9:1	10:1
<b>Years Ended December 31:</b>			
Cash used in operating activities	\$(13,500)	\$(22,921)	\$(23,912)
Cash provided by investing activities	\$ 4,081	\$ 22,533	\$ 7,977
Cash provided by financing activities	\$ 9,890	\$ 4,067	\$ 14,566

---

## Index to Financial Statements

At December 31, 2006, we had \$13.7 million of cash, cash equivalents, and marketable securities compared to \$17.4 million at December 31, 2005.

Our operating activities used \$13.5 million during 2006. This consisted primarily of the net loss for the period of \$15.8 million reduced by \$1.0 million related to changes in prepaid expenses, receivables, other assets, accounts payable and other accrued liabilities. This was offset in part by non-cash charges of \$0.4 million related to depreciation and amortization expenses and \$0.9 million related to stock based compensation expenses. Uses of cash in operating activities were primarily to fund product development programs and administrative expenses. We have entered into various agreements with research institutions, universities, and other entities for the performance of research and development activities and for the acquisition of licenses related to those activities. Certain of the licenses require us to pay royalties on future product sales, if any. In addition, in order to maintain license and other rights while products are under development, we must comply with customary licensee obligations, including the payment of patent related costs, annual minimum license fees, meeting project-funding milestones and diligent efforts in product development. The aggregate commitments we have under these agreements, including minimum license payments, for the next 12 months is approximately \$0.2 million.

Net cash provided by investing activities of \$4.1 million during 2006 consisted primarily of maturities of marketable securities of \$19.7 million, partially offset by purchases of marketable securities of \$15.6 million and capital expenditures of approximately \$0.1 million.

Net cash provided by financing activities during 2006 was \$9.9 million, which consisted primarily of \$9.3 million of net proceeds from the sale of common stock under an existing shelf registration statement and net proceeds from the exercise of stock options.

On September 28, 2005, we entered into a Standby Equity Distribution Agreement with Cornell Capital Partners. Under the agreement, we can require Cornell to purchase up to \$35.0 million of our common stock over a two year period following the effective date of a registration statement covering the shares of the common stock to be sold to Cornell Capital Partners. We can make draw-downs under the agreement in \$2.0 million increments. At the closing of each draw-down (which will take place six days after our notification to Cornell Capital Partners) we will issue to Cornell Capital Partners a number of shares of our common stock equal to the amount of the draw-down divided by the lowest daily volume weighted average price of our common stock during the five trading days following the draw-down notice to Cornell Capital Partners. At each closing, we will pay 5% of the amount of the draw-down to Cornell Capital Partners and \$500 to Yorkville Associates Management, the investment advisor to Cornell Capital Partners. We are not obligated to make any draw-downs under the agreement, and will not pay any additional fees to Cornell Capital Partners if we do not do so. As of December 31, 2006, we completed a total of five draw-downs under the Standby Equity Distribution Agreement pursuant to which we issued an aggregate of 3,131,228 shares and received net proceeds of approximately \$3.8 million. We can issue 3,344,059 additional shares under the agreement without receipt of the required shareholder approval. We did not make any draw-downs under this facility in 2006.

In February 2004, we filed a shelf registration statement with the Securities and Exchange Commission to sell up to \$50 million of common or preferred stock. Under this registration statement, shares may be sold periodically to provide additional funds for our operations. In March 2004, we completed a sale of 3,075,000 shares of our common stock offered under the registration statement at a price of \$5.00 per share, for gross proceeds of approximately \$15.4 million. Net proceeds were approximately \$14.4 million. In March 2006, we completed a sale of 3,076,924 shares of our common stock offered under the registration statement at a price of \$3.25 per share, for gross proceeds of approximately \$10 million. Net proceeds were approximately \$9.3 million. This shelf registration statement expired in February 2007.

In February 2007, we filed a shelf registration statement with the Securities and Exchange Commission to sell up to \$50 million of common or preferred stock. Under this registration statement, shares may be sold periodically to provide additional funds for our operations.

We expect to continue to incur substantial additional operating losses from costs related to continuation of product and technology development, clinical trials, and administrative activities. We believe that with our current cash balances and the Standby Equity Distribution agreement we will have access to sufficient working capital to sustain our planned operations through the end of 2007.

Although the Standby Equity Distribution agreement provides us with up to an additional \$31.0 million of financing, subject to the receipt of required shareholder approval, we will need to seek additional financing sources to fund our product development activities, and will be required to obtain substantial funding to commercialize any products other than iloperidone or Spheramine that we may successfully develop. If we are unable to complete a debt or equity offering, or otherwise obtain sufficient financing when and if needed, we may be required to reduce, defer or discontinue one or more of our product development programs.

## Index to Financial Statements

The following table sets forth the aggregate contractual cash obligations as of December 31, 2006 (in thousands):

Contractual obligations	Payments Due by Period				
	Total	< 1 year	1-3 years	3-5 years	5 years+
Operating leases	\$2,103	\$ 636	\$ 1,171	\$ 296	—
Sponsored research & license agreements	\$ 779	\$ 133	\$ 238	\$ 272	\$ 136
Total contractual cash obligations	<u>\$2,882</u>	<u>\$ 769</u>	<u>\$ 1,409</u>	<u>\$ 568</u>	<u>\$ 136</u>

For a full discussion of risks and uncertainties regarding our need for additional financing, see “Risk Factors—We will need additional financing.”

### **Off-Balance Sheet Arrangements**

We have never entered into any off-balance sheet financing arrangements and we have never established any special purpose entities. We have not guaranteed any debt or commitments of other entities or entered into any options on non-financial assets.

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

Our portfolio of marketable securities exposes us to interest rate risk. We adhere to an investment policy that requires us to limit amounts invested in securities based on maturity, type of instrument, investment grade and issuer. We satisfy liquidity requirements by investing excess cash in securities with different maturities to match projected cash needs and limit concentration of credit risk by diversifying our investments among a variety of high credit-quality issuers. A hypothetical 100 basis point decrease in interest rates would result in an approximate \$100,000 decrease in cash flow over the subsequent year. We do not use derivative financial instruments in our investment portfolio.

The following table summarizes principal amounts and related weighted-average interest rates by year of maturity on our interest-bearing investment portfolio at December 31, 2006 (in thousands, except interest rate):

Cash equivalents and marketable securities:	Face Value			Estimated Fair value
	2007	2008	Total	
Variable rate securities	\$7,560	—	\$7,560	\$ 7,560
Average interest rate	5.06%	—	5.06%	
Fixed rate securities	\$3,400	\$ 702	\$4,102	\$ 4,102
Average interest rate	4.09%	3.79%	4.04%	

### **Item 8. Consolidated Financial Statements and Supplementary Data.**

The response to this item is included in a separate section of this Report. See “Index to Consolidated Financial Statements” on Page F-1.

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

None.

### **Item 9A. Controls and Procedures.**

(a) *Evaluation of Disclosure Controls and Procedures*: Our principal executive and financial officers reviewed and evaluated our disclosure controls and procedures (as defined in Exchange Act Rule 13a-15(e)) as of the end of the period covered by this Form 10-K. Based on that evaluation, our principal executive and financial officers concluded that our disclosure controls and procedures are effective in timely providing them with material information relating to the Company, as required to be disclosed in the reports we file under the Exchange Act.

(b) *Management’s Annual Report on Internal Control Over Financial Reporting*: Our management is responsible for establishing and maintaining adequate internal control over our financial reporting. Management assessed the effectiveness of our internal control over financial reporting as of December 31, 2006. In making this assessment, management used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission in *Internal Control—Integrated Framework*. Based on the assessment using those criteria, management concluded that, as of December 31, 2006, our internal control over financial reporting was effective.



---

## [Index to Financial Statements](#)

Our independent registered public accounting firm, Odenberg, Ullakko, Muranishi & Co. LLP, have issued an attestation report on management's assessment of our internal control over financial reporting as well as on the effectiveness of our internal control over financial reporting as of December 31, 2006. The attestation report on the internal control over financial reporting appears elsewhere in this Annual Report on Form 10-K.

(c) *Changes in Internal Control Over Financial Reporting*: There were no changes in our internal control over financial reporting during the year that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

### **Item 9B. Other Information.**

None.

**PART III**

**Item 10. Directors, Executive Officers and Corporate Governance.**

Set forth below are the name, age and position and a brief account of the business experience of each of our executive officers and directors as of March 1, 2006.

<u>Name</u>	<u>Age</u>	<u>Office</u>
Louis R. Bucalo, M.D.(1)	48	Chairman, President and Chief Executive Officer
Sunil Bhonsle	57	Executive Vice President, Chief Operating Officer and Director
Robert E. Farrell, J.D.	57	Executive Vice President and Chief Financial Officer
Victor J. Bauer, Ph.D.	71	Director
Eurelio M. Cavalier(1)(3)(4)	74	Director
Hubert E. Huckel, M.D.(1)(2)(3)	75	Director
Joachim Friedrich Kapp, M.D., Ph.D.	64	Director
M. David MacFarlane, Ph.D.(2)(4)	66	Director
Ley S. Smith(1)(2)(4)	72	Director
Konrad M. Weis, Ph.D.(1)(3)	78	Director

- (1) Member of Executive Committee
- (2) Member of Audit Committee
- (3) Member of Compensation Committee
- (4) Member of Nominating Committee

**Louis R. Bucalo, M.D.** is the founder of Titan and has served as our President and Chief Executive Officer since January 1993. Dr. Bucalo has served as a director of Titan since March 1993 and was elected Chairman of the Board of Directors in January 2000. From July 1990 to April 1992, Dr. Bucalo was Associate Director of Clinical Research at Genentech, Inc., a biotechnology company. Dr. Bucalo holds an M.D. from Stanford University and a B.A. in biochemistry from Harvard University.

**Sunil Bhonsle** has served as our Executive Vice President and Chief Operating Officer since September 1995, and has served as a director of Titan since February 2004. Mr. Bhonsle served in various positions, including Vice President and General Manager—Plasma Supply and Manager—Inventory and Technical Planning, at Bayer Corporation from July 1975 until April 1995. Mr. Bhonsle holds an M.B.A. from the University of California at Berkeley and a B.Tech. in chemical engineering from the Indian Institute of Technology.

**Robert E. Farrell, J.D.** has served as our Executive Vice President and Chief Financial Officer since September 1996. Mr. Farrell was employed by Fresenius USA, Inc. from 1991 until August 1996 where he served in various capacities, including Vice President Administration, Chief Financial Officer and General Counsel. His last position was Corporate Group Vice President. Mr. Farrell holds a B.A. from the University of Notre Dame and a J.D. from Hastings College of Law, University of California.

**Victor J. Bauer, Ph.D.** has served on our Board of Directors since November 1997. Dr. Bauer serves as the Executive Vice President of Concordia Pharmaceuticals, Inc., a biopharmaceutical company he co-founded in January 2004. From February 1997 through March 2003, Dr. Bauer was employed by Titan, most recently as our Executive Director of Corporate Development. From April 1996 until its merger into Titan, Dr. Bauer also served as a director and Chairman of Theracell. From December 1992 until February 1997, Dr. Bauer was a self-employed consultant to companies in the pharmaceutical and biotechnology industries. Prior to that time, Dr. Bauer was with Hoechst-Roussel Pharmaceuticals Inc., where he served as President from 1988 through 1992.

**Eurelio M. Cavalier** has served on our Board of Directors since September 1998. He was employed in various capacities by Eli Lilly & Co. from 1958 until his retirement in 1994, serving as Vice President Sales from 1976 to 1982 and Group Vice President U.S. Pharmaceutical Business Unit from 1982 to 1993. Mr. Cavalier currently serves on the Board of Directors of ProSolv, Inc.

**Hubert E. Huckel, M.D.** has served on our Board of Directors since October 1995. He served in various positions with The Hoechst Group from 1964 until his retirement in December 1992. At the time of his retirement, Dr. Huckel was Chairman of the Board of Hoechst-Roussel Pharmaceuticals, Inc., Chairman and President of Hoechst-Roussel Agri-Vet Company and a member of the Executive

---

## [Index to Financial Statements](#)

Committee of Hoechst Celanese Corporation. He currently serves on the Board of Directors of ThermoGenesis Corp., Valera Pharmaceuticals, Inc., Catalyst Pharmaceuticals, Inc. and Concordia Pharmaceuticals, Inc. He is a member of the compensation committee of ThermoGenesis Corp.

**Joachim Friedrich Kapp, M.D., Ph.D.** has served on our Board of Directors since August 2005. Dr. Kapp has worked in various capacities for Schering AG since 1975, from 1991 on as President of the Global Business Unit, Specialized Therapeutics. Dr. Kapp worked in various capacities with Warner Lambert and its subsidiaries between 1984 and 1990. Dr. Kapp holds an M.D. and a Ph.D. from The University of Essen, Germany.

**M. David MacFarlane, Ph.D.** has served on the Board of Directors since May 2002. From 1989 until his retirement in August 1999, Dr. MacFarlane served as Vice President and Responsible Head of Regulatory Affairs of Genentech, Inc. Prior to joining Genentech, Inc., he served in various positions with Glaxo Inc., last as Vice President of Regulatory Affairs.

**Ley S. Smith** has served on our Board of Directors since July 2000. He served in various positions with The Upjohn Company and Pharmacia & Upjohn from 1958 until his retirement in November 1997. From 1991 to 1993 he served as Vice Chairman of the Board of The Upjohn Company, and from 1993 to 1995 he was President and Chief Operating Officer of The Upjohn Company. At the time of his retirement, Mr. Smith was Executive Vice President of Pharmacia & Upjohn, and President of Pharmacia & Upjohn's U.S. Pharma Product Center.

**Konrad M. Weis, Ph.D.** has served on our Board of Directors since March 1993. He is the former President, Chief Executive Officer and Honorary Chairman of Bayer Corporation. Since 1995, Dr. Weis has been serving as a director and member of the Investment Committee of The Heinz Endowment in Pittsburgh. Since 2004, he has been serving as Emeritus Life Trustee of Carnegie-Mellon University and its Executive Committee, and of the Carnegie Museums of Pittsburgh.

Directors serve until the next annual meeting or until their successors are elected and qualified. Officers serve at the discretion of the Board of Directors, subject to rights, if any, under contracts of employment. See "Item 11. Executive Compensation—Employment Agreements."

### **Code of Ethics**

We have adopted a Code of Business Conduct and Ethics (the "Code") that applies to our directors, officers and employees, including our Chief Executive Officer and Chief Financial Officer (our principal executive officer and principal financial and accounting officer, respectively). The Code was filed as Exhibit 14 to our annual report on Form 10-K for the year ended December 31, 2003 and has been incorporated by reference into this annual report. A written copy of the Code will be provided upon request at no charge by writing to our Chief Financial Officer, Titan Pharmaceuticals, Inc., 400 Oyster Point Boulevard, Suite 505, South San Francisco, California 94080.

### **Formation of Audit Committee and Financial Expert**

The Audit Committee (which is formed in compliance with Section 3(a)(58)(A) of the Securities Exchange Act of 1934) consists of Ley S. Smith, M. David MacFarlane and Hubert E. Huckel, each of whom meets the independence requirements and standards currently established by the American Stock Exchange and the SEC. In addition, the Board of Directors has determined that Mr. Ley Smith is an "audit committee financial expert" and "independent" as defined under the relevant rules of the SEC and the American Stock Exchange.

### **Changes in Director Nomination Process for Stockholders**

None.

### **Section 16(a) Beneficial Ownership Reporting Compliance**

Section 16(a) of the Securities Exchange Act of 1934, as amended (the "Exchange Act"), requires our executive officers, directors and persons who beneficially own more than 10% of a registered class of our equity securities to file with the Securities and Exchange Commission initial reports of ownership and reports of changes in ownership of our common stock and other equity securities. Such executive officers, directors, and greater than 10% beneficial owners are required by SEC regulation to furnish us with copies of all Section 16(a) forms filed by such reporting persons.

Based solely on our review of such forms furnished to us and written representations from certain reporting persons, we believe that all filing requirements applicable to our executive officers, directors and greater than 10% beneficial owners were complied with during 2006.

## **Item 11. Executive Compensation.**

### **Overview**

This compensation discussion describes the material elements of compensation awarded to, earned by, or paid to each of our executive officers who served as named executive officers during the last completed fiscal year. This compensation discussion focuses on the information contained in the following tables and related footnotes and narrative for primarily the last completed fiscal year, but we also describe compensation actions taken before or after the last completed fiscal year to the extent it enhances the understanding of our executive compensation disclosure.

Our Compensation Committee currently oversees the design and administration of our executive compensation program.

The principal elements of our executive compensation program are base salary, annual cash incentives, long-term equity incentives in the form of stock options, other benefits and perquisites, post-termination severance and acceleration of stock option vesting for certain named executive officers upon termination and/or a change in control. Our other benefits and perquisites consist of life, health and disability insurance benefits, and a qualified 401(k) savings plan. Our philosophy is to position the aggregate of these elements at a level that is competitive within the industry and commensurate with our size and performance.

### **Compensation Program Objectives and Philosophy**

*In General.* The objectives of our compensation programs are to:

- attract, motivate and retain talented and dedicated executive officers,
- provide our executive officers with both cash and equity incentives to further our interests and those of our stockholders, and
- provide employees with long-term incentives so we can retain them and provide stability during our growth stage.

Generally, the compensation of our executive officers is composed of a base salary, an annual incentive compensation award and equity awards in the form of stock options based on individual and company performance. In adjusting base salaries, the Compensation Committee reviews the individual contributions of the particular executive. The annual incentive compensation award is a discretionary award determined by the Compensation Committee based on company performance. In addition, stock options are granted to provide the opportunity for long-term compensation based upon the performance of our common stock over time.

*Competitive Market.* We define our competitive markets for executive talent to be the pharmaceutical and biotechnology industries in northern California and New Jersey. To date, we have utilized the Radford Biotechnology Surveys, a third party market specific compensation survey, to benchmark our executive compensation.

*Compensation Process.* The Compensation Committee reviews and approves all elements of compensation for each of our named executive officers taking into consideration recommendations from our principal executive officer (for compensation other than his own), as well as competitive market guidance from the Radford Biotechnology Surveys.

### **Base Salaries**

*In General.* We provide the opportunity for our named executive officers and other executives to earn a competitive annual base salary to attract and retain an appropriate caliber of talent for the applicable position, and to provide a base wage that is not subject to our performance risk. We review base salaries for our named executive officers annually and cost of living increases and other changes are based on compensation surveys, the Company's performance and individual performance, such as meeting product development and corporate objectives. The salary of our principal executive officer and the salaries of our named executive officers are set by the Compensation Committee.

*Total Compensation Comparison.* Base salaries accounted for approximately 73% of total compensation for the principal executive officer and approximately 81% on average for our other named executive officers.

### **Annual Cash Incentives**

*In General.* We provide the opportunity for our named executive officers and other executives to earn an annual cash incentive award. We provide this opportunity to attract and retain an appropriate caliber of talent for the position and to motivate executives to achieve our annual business goals. We review potential annual cash incentive awards for our named executive officers and other executives annually to determine award payments, if any, for the last completed fiscal year, as well as to establish award opportunities for the current fiscal year. We do not have a formal annual incentive plan and payment of annual cash incentive awards are subject to the discretion of the Compensation Committee.

## [Index to Financial Statements](#)

**Target Award Opportunities.** Our 2006 cash incentive awards were subject to the Compensation Committee's discretion and took into account corporate performance measures, including, but not limited to, product development milestones and results of operations. There are annual target award opportunities expressed as a percentage of base salary paid during the fiscal year as specified in the employment agreements. For the last completed fiscal year, annual cash incentive opportunities for the named executive officers are summarized below. There were no cash bonuses paid to our named executive officers during or related to 2006.

		Annual Cash Incentive Award Opportunity		
		Target Performance		Amount Paid
		% Salary	Amount	
Louis R. Bucalo, M.D.	FY 2006	25%	\$ 94,490	\$ —
Sunil Bhonsle	FY 2006	20%	\$ 57,582	\$ —
Robert E. Farrell	FY 2006	20%	\$ 48,067	\$ —
Richard C. Allen, Ph.D. (1)	FY 2006	20%	\$ —	\$ —

(1) Dr. Allen's employment terminated in March 2006.

**Individual Performance Goals.** The performance goals for the executives are aligned with the objectives for the Company and seek to advance our product development goals. The Compensation Committee takes into account individual and Company performance in determining awards.

**Discretionary Adjustments.** Incentive awards are subject to the Compensation Committee's discretion. We may make adjustments to our overall corporate performance goals and our actual performance results that may cause differences between the numbers used for our performance goals and the numbers reported in our financial statements. These adjustments may exclude all or a portion of both the positive or negative effect of external events that are outside the control of our executives, such as natural disasters, litigation, or regulatory changes in accounting or taxation standards. These adjustments may also exclude all or a portion of both the positive or negative effect of unusual or significant strategic events that are within the control of our executives but that are undertaken with an expectation of improving our long-term financial performance, such as restructurings, acquisitions, or divestitures.

**Total Compensation Comparison.** For the last completed fiscal year, cash incentive awards accounted for none of the total compensation for the principal executive officer and our other named executive officers.

### Long-term Equity Incentives

We provide the opportunity for our named executive officers and other executives to earn a long-term equity incentive award. Long-term incentive awards provide employees with the incentive to stay with us for longer periods of time, which in turn, provides us with greater stability. Equity awards also are less costly to us in the short term than cash compensation. We review long-term equity incentives for our named executive officers and other executives annually.

For our named executive officers, our stock option grants are of a size and term determined and approved by the Compensation Committee in consideration of the range of grants in the Radford Survey. We have traditionally used stock options as our form of equity compensation because stock options provide a relatively straightforward incentive for our executives, result in less immediate dilution of existing shareholders' interests and, prior to our adoption of FAS 123(R), resulted in less compensation expense for us relative to other types of equity awards. Generally, all grants of stock options to our employees were granted with exercise prices equal to or greater than the fair market value of our common stock on the respective grant dates. For a discussion of the determination of the fair market value of these grants, see "Management's Discussion and Analysis of Financial Condition and Results of Operations—Critical Accounting Policies and the Use of Estimates."

We do not time stock option grants to executives in coordination with the release of material non-public information. For the last two years, annual grants to employees (including executive officers) have been made on the first business day of the year. Beginning with annual grants for 2007, the grants will be made on the first Monday in January that is a business day. Initial Director option grants may be granted on the date the Director joins the Board of Directors. Biennial Director option grants are granted automatically upon election at the annual shareholder meeting. Director committee option grants are made at the first meeting of the Board of Directors after Titan's annual shareholder meeting. We also make automatic option grants on the five and ten year anniversary date of an employee's employment. Newly-hired employees may be granted options on the first day of employment. Our stock option grants have a 10-year contractual exercise term. In general, the option grants are also subject to the following post-termination and change in control provisions:

## Index to Financial Statements

Event	Award Vesting	Exercise Term
• Termination by us for Reason Other than Cause, Disability or Death	• Forfeit Unvested Options	• Earlier of: (1) 90 days or (2) Remaining Option Period
• Termination for Disability, Death or Retirement	• Forfeit Unvested Options	• Earlier of: (1) 2 years or (2) Remaining Option Period
• Termination for Cause	• Forfeit Vested and Unvested Options	• Expire
• Other Termination	• Forfeit Unvested Options	• Earlier of: (1) 90 days or (2) Remaining Option Period
• Change in Control	• Accelerated*	•*

\* The Compensation Committee may provide that, in the event of a change in control, any outstanding awards that are unexercisable or otherwise unvested will become fully vested and immediately exercisable. If there is a termination of employment, the applicable termination provisions regarding exercise term will apply.

The vesting of certain of our named executive officers' stock options is accelerated pursuant to the terms of their employment agreements in certain termination and/or change in control events. These terms are more fully described in "—Employment Agreements" and "—Potential Payments upon Termination or Change in Control."

**Total Compensation Comparison.** Long-term equity incentives accounted for approximately 27% of total compensation for the principal executive officer and approximately 19% on average for our other named executive officers.

### Executive Benefits and Perquisites

**In General.** We generally provide for our named executive officers and other executives to receive the same general health and welfare benefits offered to all employees. We currently provide no other perquisites to our named executive officers and other executives. We also offer participation in our defined contribution 401(k) plan. We do not match employee contributions under our 401(k) plan.

**Total Compensation Comparison.** Personal benefits and perquisites accounted for approximately 1% of total compensation for the principal executive officer and our other named executives officers.

### Change in Control and Severance Benefits

**In General.** We provide the opportunity for certain of our named executive officers to be protected under the severance and change in control provisions contained in their employment agreements. We provide this opportunity to attract and retain an appropriate caliber of talent for the applicable position. Our severance and change in control provisions for the named executive officers are summarized in "—Employment Agreements" and "—Potential Payments upon Termination or Change in Control." Our analysis indicates that our severance and change in control provisions are consistent with the provisions and benefit levels of other companies disclosing such provisions as reported in public SEC filings. We believe our arrangements are reasonable in light of the fact that cash severance is limited to the greater of the term of the agreement or two years for the Principal Executive Officer (at a rate equal to his then current base salary) and nine months for other named executive officers (at a rate equal to their then current base salary), there is no severance increase with a change in control and there are no "single trigger" benefits upon a change in control.

## [Index to Financial Statements](#)

### Compensation Committee Interlocks and Insider Participation

Members of our Compensation Committee of the Board of Directors were Mr. Eurelio M. Cavalier, Dr. Hubert E. Huckel and Dr. Konrad M. Weis. No member of our Compensation Committee was, or has been, an officer or employee of Titan or any of our subsidiaries.

No member of the Compensation Committee has a relationship that would constitute an interlocking relationship with executive officers or directors of the Company or another entity.

### Compensation Committee Report (1)

The goal of the Company's executive compensation policy is to ensure that an appropriate relationship exists between executive compensation and the creation of stockholder value, while at the same time attracting, motivating and retaining experienced executive officers.

The Compensation Committee has reviewed and discussed the discussion and analysis of Titan's compensation which appears above with management, and, based on such review and discussion, the Compensation Committee recommended to Titan's Board of Directors that the above disclosure be included in this Annual Report on Form 10-K.

The members of the Compensation Committee are:

Eurelio M. Cavalier, Chair  
Hubert E. Huckel, M.D.  
Konrad M. Weis, Ph.D.

- (1) The material in the above Audit and Compensation Committee reports is not soliciting material, is not deemed filed with the SEC and is not incorporated by reference in any filing of the Company under the Securities Act of 1933, or the Securities Exchange Act of 1934, whether made before or after the date of this Form 10-K and irrespective of any general incorporation language in such filing.

### EXECUTIVE COMPENSATION

The following table shows information concerning the annual compensation for services provided to us by our Chief Executive Officer, the Chief Financial Officer and our three other most highly compensated executive officers during 2006.

#### SUMMARY COMPENSATION TABLE

Name and Principal Position	Year	Salary (\$)	Bonus (1) (\$)	Option Awards (2) (\$)	All Other Compensation (3) (\$)	Total Compensation (\$)
Louis R. Bucalo, M.D. President and Chief Executive Officer	2006	378,471	—	137,919	—	516,390
Sunil Bhonsle Executive Vice President and Chief Operating Officer	2006	288,421	—	87,763	—	376,184
Robert E. Farrell Executive Vice President and Chief Financial Officer	2006	240,846	—	55,484	—	296,330
Richard C. Allen, Ph.D. (4) Executive Vice President, Cell Therapy	2006	246,009	—	36,102	—	282,111

- (1) No bonuses were paid to our named executive officers during or related to 2006.

## Index to Financial Statements

- (2) Valuation based on the dollar amount of option grants recognized for financial statement reporting purposes pursuant to FAS 123(R) with respect to 2006. The assumptions used by us with respect to the valuation of option grants are set forth in “Titan Pharmaceuticals, Inc. Consolidated Financial Statements—Notes to Financial Statements—Note 1—Organization and Summary of Significant Accounting Policies—Stock Option Plans.” The individual awards reflected in the summary compensation table are summarized below:

	Grant Date	Number of Shares	Amount Recognized in Financial Statements in 2006
Louis R. Bucalo, M.D.	1/3/2006	195,000	\$ 82,543
	8/29/2006	20,000	2,695
	9/5/2006	5,000	2,556
Sunil Bhonsle	1/3/2006	135,000	56,006
	8/29/2006	20,000	2,695
Robert E. Farrell	1/3/2006	67,500	28,239
	9/21/2006	45,000	8,562
Richard C. Allen, Ph.D.	1/3/2006	57,000	23,647

- (3) No other compensation, including perquisites, in excess of \$10,000 was paid to any of our named executive officers during 2006.
- (4) Dr. Allen’s employment was terminated in March 2006. He received salary continuation payments until December 2006. Dr. Allen’s outstanding options will continue to vest under the terms of his consulting agreement through February 2008.

For a description of the material terms of employment agreements with our named executive officers, see “—Employment Agreements.”

### GRANTS OF PLAN-BASED AWARDS (1)

The following table summarizes our awards made to our named executive officers under any plan in 2006.

Name	Grant Date	Approval Date (2)	Number of Shares of Common Stock Underlying Options (#)		Exercise or Base Price of Option Awards (\$/Sh)	Grant Date Fair Value of Stock and Option Awards (\$)(3)	Grant Date Fair Market Value of a Share (\$/Sh)
Louis R. Bucalo, M.D.	1/3/2006	12/29/2005	195,000	(4)	\$ 1.40	\$163,137	\$ 0.84
	8/29/2006	8/29/2006	20,000	(5)	2.35	31,752	1.59
	9/5/2006	9/5/2006	5,000	(6)	2.48	7,975	1.60
Sunil Bhonsle	1/3/2006	12/29/2005	135,000	(4)	1.40	112,941	0.84
	8/29/2006	8/29/2006	20,000	(5)	2.48	31,752	1.59
Robert E. Farrell	1/3/2006	12/29/2005	67,500	(4)	1.40	56,471	0.84
	9/21/2006	9/21/2006	45,000	(4)	2.09	61,547	1.37
Richard C. Allen, Ph.D.(7)	1/3/2006	12/29/2005	57,000	(4)	1.40	47,686	0.84

- (1) Each award was granted under the Titan Pharmaceuticals, Inc. 2002 Stock Option Plan.
- (2) All grants were approved by the Compensation Committee on the dates indicated to be granted on the indicated grant date.
- (3) Valuation assumptions are found under “Titan Pharmaceuticals, Inc. Consolidated Financial Statements —Notes to Financial Statements —Note 1—Organization and Summary of Significant Accounting Policies—Stock Option Plans.”
- (4) These options vest over a two year period with fifty percent vesting on the first anniversary and the remaining fifty percent vesting in twelve equal monthly installments.
- (5) These options vest in forty-eight equal monthly installments beginning on August 29, 2006.
- (6) These options vest in twelve equal monthly installments beginning on September 5, 2006.



---

## [Index to Financial Statements](#)

- (7) Dr. Allen's employment was terminated in March 2006. Dr. Allen's outstanding options will continue to vest under the terms of his consulting agreement through February 2008.

### **Employee Benefits Plans**

#### *Stock Option Plans*

The principal purpose of the Stock Option Plans is to attract, motivate, reward and retain selected employees, consultants and directors through the granting of stock-based compensation awards. The Stock Option Plans provides for a variety of awards, including non-qualified stock options, incentive stock options (within the meaning of Section 422 of the Code), stock appreciation rights, restricted stock awards, performance-based awards and other stock-based awards.

#### *2002 Stock Option Plan*

In July 2002, we adopted the 2002 Stock Option Plan (2002 Plan). The 2002 Plan assumed the options which remain available for grant under our option plans previously approved by stockholders. Under the 2002 Plan and predecessor plans, a total of approximately 6.4 million shares of our common stock were authorized for issuance to employees, officers, directors, consultants, and advisers. Options granted under the 2002 Plan and predecessor plans may either be incentive stock options within the meaning of Section 422 of the Internal Revenue Code and/or options that do not qualify as incentive stock options; however, only employees are eligible to receive incentive stock options. Options granted under the option plans generally expire no later than ten years from the date of grant, except when the grantee is a 10% shareholder, in which case the maximum term is five years from the date of grant. Options generally vest at the rate of one fourth after one year from the date of grant and the remainder ratably over the subsequent three years, although options with different vesting terms are granted from time-to-time. Generally, the exercise price of any options granted under the 2002 Plan must be at least 100% of the fair market value of our common stock on the date of grant, except when the grantee is a 10% shareholder, in which case the exercise price shall be at least 110% of the fair market value of our common stock on the date of grant.

In August 2005, we adopted an amendment to the 2002 Stock Option Plan (2002 Plan) to (i) permit the issuance of Shares of restricted stock and stock appreciation rights to participants under the 2002 Plan, and (ii) increase the number of Shares issuable pursuant to grants under the 2002 Plan from 2,000,000 to 3,000,000.

#### *2001 Stock Option Plan*

In August 2001, we adopted the 2001 Employee Non-Qualified Stock Option Plan (2001 NQ Plan) pursuant to which 1,750,000 shares of common stock were authorized for issuance for option grants to employees and consultants who are not officers or directors of Titan. Options granted under the option plans generally expire no later than ten years from the date of grant. Option vesting schedule and exercise price are determined at time of grant by the Board of Directors. Generally, the exercise prices of options granted under the 2001 NQ Plan were 100% of the fair market value of our common stock on the date of grant.

*Administration.* The Stock Option Plans are administered by our Compensation Committee. The Compensation Committee may in certain circumstances delegate certain of its duties to one or more of our officers. The Compensation Committee has the power to interpret the Stock Option Plans and to adopt rules for the administration, interpretation and application of the plans according to their terms.

*Grant of Awards; Shares Available for Awards.* Certain employees, consultants and directors are eligible to be granted awards under the plans. The Compensation Committee will determine who will receive awards under the plans, as well as the form of the awards, the number of shares underlying the awards, and the terms and conditions of the awards consistent with the terms of the plans.

A total of approximately 8.3 million shares of our common stock are available for issuance or delivery under our existing Stock Option Plans. The number of shares of our common stock issued or reserved pursuant to the Stock Option Plans will be adjusted at the discretion of our Board or the Compensation Committee as a result of stock splits, stock dividends and similar changes in our common stock. In addition, shares subject to grant under our prior option plans (including shares under such plans that expire unexercised or are forfeited, terminated, canceled or withheld for income tax withholding) shall be merged and available for issuance under the 2002 Stock Option Plan, without reducing the aggregate number of shares available for issuance reflected above.

*Stock Options.* The Stock Option Plans permit the Compensation Committee to grant participants incentive stock options, which qualify for special tax treatment in the United States, as well as non-qualified stock options. The Compensation Committee will establish the duration of each option at the time it is granted, with a maximum ten-year duration for incentive stock options, and may also establish vesting and performance requirements that must be met prior to the exercise of options. Stock option grants (other than incentive stock option grants) also may have exercise prices that are

## Index to Financial Statements

less than, equal to or greater than the fair market value of our common stock on the date of grant. Incentive stock options must have an exercise price that is at least equal to the fair market value of our common stock on the date of grant. Stock option grants may include provisions that permit the option holder to exercise all or part of the holder's vested options, or to satisfy withholding tax liabilities, by tendering shares of our common stock already owned by the option holder for at least six months (or another period consistent with the applicable accounting rules) with a fair market value equal to the exercise price.

*Stock Appreciation Rights.* The Compensation Committee may also grant stock appreciation rights, which will be exercisable upon the occurrence of certain contingent events. Stock appreciation rights entitle the holder upon exercise to receive an amount in any combination of cash, shares of our common stock (as determined by the Compensation Committee) equal in value to the excess of the fair market value of the shares covered by the stock appreciation right over the exercise price of the right, or other securities or property owned by us.

*Other Equity-Based Awards.* In addition to stock options and stock appreciation rights, the Compensation Committee may also grant certain employees, consultants and directors shares of restricted stock, with terms and conditions as the Compensation Committee may, pursuant to the terms of the Stock Option Plan, establish. The Stock Option Plan does not allow awards to be made under terms and conditions which would cause such awards to be treated as deferred compensation subject to the rules of Section 409A of the Code.

*Change-in-Control Provisions.* In connection with the grant of an award, the Compensation Committee may provide that, in the event of a change in control, any outstanding awards that are unexercisable or otherwise unvested will become fully vested and immediately exercisable.

*Amendment and Termination.* The Compensation Committee may adopt, amend and rescind rules relating to the administration of the Stock Option Plans, and amend, suspend or terminate the Stock Option Plans, but no amendment will be made that adversely affects in a material manner any rights of the holder of any award without the holder's consent, other than amendments that are necessary to permit the granting of awards in compliance with applicable laws. We have attempted to structure the Stock Option Plans so that remuneration attributable to stock options and other awards will not be subject to a deduction limitation contained in Section 162(m) of the Code.

### OUTSTANDING EQUITY AWARDS AT FISCAL YEAR-END

The following table summarizes the number of securities underlying outstanding plan awards for each named executive officer as of December 31, 2006.

Name	Option Awards			
	Number of Securities Underlying Unexercised Options (#) Exercisable	Number of Securities Underlying Unexercised Options (#) Unexercisable	Option Exercise Price (\$)	Option Expiration Date
Louis R. Bucalo, M.D.	2,000	—	\$ 2.88	7/30/2007
	59,200	—	5.30	6/10/2008
	433,088	—	7.50	6/19/2008
	5,000	—	4.14	7/24/2008
	71,500	—	3.63	1/4/2009
	28,000	—	3.69	2/4/2009
	27,531	—	0.08	3/10/2009
	5,000	—	9.06	8/30/2009
	400,000	—	12.69	11/23/2009
	20,000	—	43.63	8/28/2010
	72,000	—	22.98	1/8/2011
	69,000	—	11.63	8/9/2011
	5,000	—	11.50	8/10/2011
	150,000	—	8.77	1/16/2012
	20,000	—	1.71	8/16/2012

## Index to Financial Statements

	80,000	—	1.50	3/1/2013
	5,000	—	3.29	10/31/2013
	75,000	—	3.69	2/9/2014
	13,437	6,563(1)	2.37	9/1/2014
	50,000	50,000(2)	2.62	2/7/2015
	5,000	—	2.05	8/9/2015
	—	195,000(3)	1.40	1/3/2016
	1,666	18,334(4)	2.35	8/29/2016
	1,250	3,750(5)	2.48	9/5/2016
Sunil Bhonsle	41,600	—	5.30	6/10/2008
	165,158	—	7.50	6/19/2008
	55,600	—	3.63	1/4/2009
	21,000	—	3.69	2/4/2009
	184,000	—	12.69	11/23/2009
	42,000	—	22.98	1/8/2011
	31,500	—	11.63	8/9/2011
	90,000	—	8.77	1/16/2012
	50,000	—	1.50	3/1/2013
	60,000	—	3.69	2/9/2014
	35,000	35,000(2)	2.62	2/7/2015
	—	135,000(3)	1.40	1/3/2016
	1,666	18,334(4)	2.35	8/29/2016
Robert E. Farrell	66,000	—	12.68	11/23/2009
	30,000	—	22.98	1/8/2011
	22,500	—	11.63	8/9/2011
	60,258	—	3.77	6/4/2012
	68,294	—	1.71	8/16/2012
	35,000	—	1.50	3/1/2013
	35,000	—	3.69	2/9/2014
	22,500	22,500(2)	2.62	2/7/2015
	—	67,500(3)	1.40	1/3/2016
	—	45,000(3)	2.09	9/21/2016
Richard C. Allen, Ph.D.(6)	33,300	—	5.30	6/10/2008
	61,961	—	7.50	6/19/2008
	41,200	—	3.63	1/4/2009
	21,000	—	3.69	2/4/2009
	132,000	—	12.69	11/23/2009
	36,000	—	22.98	1/8/2011
	27,000	—	11.63	8/9/2011
	85,000	—	8.77	1/16/2012
	35,000	—	1.50	3/1/2013
	30,000	—	3.69	2/9/2014
	15,000	15,000(2)	2.62	2/7/2015
	—	57,000(3)	1.40	1/3/2016

(1) These options vest in twelve equal monthly installments beginning on September 1, 2004.

(2) These options vest in two equal annual installments beginning on February 7, 2005.

---

## [Index to Financial Statements](#)

- (3) These options vest over a two year period with fifty percent vesting on the first anniversary and the remaining fifty percent vesting in twelve equal monthly installments.
- (4) These options vest in forty-eight equal monthly installments beginning on August 29, 2006.
- (5) These options vest in twelve equal monthly installments beginning on September 5, 2006.
- (6) Dr. Allen's employment was terminated in March 2006. Dr. Allen's outstanding options will continue to vest under the terms of his consulting agreement through February 2008.

There were no option exercises by our named executive officers in 2006. To date, we have not granted any stock awards to our named executive officers.

### **Pension Benefits**

We do not sponsor any qualified or non-qualified defined benefit plans.

### **Nonqualified Deferred Compensation**

We do not maintain any non-qualified defined contribution or deferred compensation plans. The Compensation Committee, which is comprised solely of "outside directors" as defined for purposes of Section 162(m) of the Code, may elect to provide our officers and other employees with non-qualified defined contribution or deferred compensation benefits if the Compensation Committee determines that doing so is in our best interests. We sponsor a tax qualified defined contribution 401(k) plan in which Dr. Bucalo, Mr. Bhonsle, and Mr. Farrell participate.

### **Employment Agreements**

#### *Employment Agreement with Louis R. Bucalo*

We are a party to an employment agreement with Dr. Bucalo which, as amended in February, 2007, expires in February 2010 and provides for a base annual salary, subject to annual increases of 5% and bonuses of up to 25% at the discretion of the Board of Directors.

Dr. Bucalo's employment agreement may be terminated, with or without just cause, by our Board. If we terminate the employment agreement for just cause (as defined in the agreement) or on account of death or disability or if Dr. Bucalo terminates the agreement for any reason other than just cause (as defined in the agreement), Dr. Bucalo is entitled to no further compensation or benefits other than those earned through the date of termination. If we terminate the agreement for any reason other than for just cause, death or disability, we provide severance of continued payment of cash compensation at a rate of his then current base annual salary for a period equal to the greater of the balance of the term of the agreement or two years, subject to offset for earnings after the first 18 months following termination.

#### *Employment Agreements with Other Executive Officers*

In addition to the employment agreement with Dr. Bucalo, we have entered into employment agreements with Sunil Bhonsle and Robert E. Farrell. The employment agreements generally provide for a base salary and eligibility to receive an annual performance bonus up to a specified percentage of base salary. The actual amount of the annual bonus is discretionary and determined based upon the executive's performance, our performance and certain performance targets approved by our Compensation Committee. The agreements also grant options to purchase shares of common stock and contain customary non-competition and non-solicitation provisions.

The agreements may be terminated, with or without good cause, by the executive, the Chief Executive Officer or our Board. If the executive's employment is terminated by us for good cause (as defined in the agreements) or if the executive terminates his own employment for any reason other than for good cause (as defined in the agreements), the executive is entitled to no further compensation or benefits other than those earned through the date of termination. If the executive's employment is terminated by us for good cause due to death or disability (as defined in the agreement) we will continue payment of the executive's base salary for six months following termination. If the executive's employment is terminated by us for any reason other than for good cause, death or disability, or if the executive terminates his own employment for good cause, we will continue payment of the executive's base salary for nine months following termination, subject to offset by other employment salary received during such period.

### POTENTIAL PAYMENTS UPON TERMINATION OR CHANGE IN CONTROL

Assuming the employment of our named executive officers were to be terminated without cause or for good reason, each as of December 31, 2006, the following individuals would be entitled to payments in the amounts set forth opposite to their name in the below table:

	Cash Severance
Louis R. Bucalo, M.D.	\$31,583 per month for 24 months
Sunil Bhonsle	\$24,058 per month for 9 months
Robert E. Farrell	\$20,083 per month for 9 months

We are not obligated to make any cash payments to these executives if their employment is terminated by us for cause or by the executive not for good reason. No severance or benefits are provided for any of the executive officers in the event of death or disability. A change in control does not affect the amount or timing of these cash severance payments.

Assuming the employment of our named executive officers were to be terminated without cause or for good reason, each as of December 31, 2006, the following individuals would be entitled to accelerated vesting of their outstanding stock options described in the table below:

	Value of Equity Awards: Termination Without Cause or For Good Reason (1)	Value of Equity Awards: In Connection With a Change in Control (1)
Louis R. Bucalo, M.D.	None	Fully Vested. 273,647 options with value of \$324,812
Sunil Bhonsle	None	Fully Vested. 188,334 options with value of \$117,116
Robert E. Farrell	None	Fully Vested. 135,000 options with value of \$189,403

(1) Values are based on the aggregate difference between the respective exercise prices and the closing sale price of our common stock on December 29, 2006, which was \$3.32 per share.

### DIRECTOR COMPENSATION

#### Summary of Director Compensation

Non-employee directors are entitled to receive a fee for each meeting attended and all directors are entitled to receive stock options pursuant to our stockholder-approved stock option plans, including an initial grant of 10,000 options upon becoming a director, a biennial grant of 20,000 options thereafter, and an annual grant of 5,000 options for each committee on which they serve. During 2006, each director was granted an annual option to purchase 5,000 shares of our common stock at an exercise price of \$2.48, which was equal to the fair market value of our common stock at date of grant, with respect to each committee of the Board on which each director served. In addition to having their out-of-pocket expenses reimbursed, non-employee directors received \$2,500 for each Board of Directors meeting attended in 2006. Directors are not precluded from serving us in any other capacity and receiving compensation therefore. Non-employee directors also receive an annual retainer fee of \$5,000 in addition to the fee received for each meeting attended.

## Index to Financial Statements

The following table summarizes compensation that our directors earned during 2006 for services as members of our Board.

Name	Fees Earned or Paid in Cash (\$)	Options Awards (\$)(1)	All Other Compensation (\$)	Total (\$)
Victor J. Bauer, Ph.D.	15,000	35,935	—	50,935
Eurelio M. Cavalier	15,000	59,860	—	74,860
Hubert Huckel, M.D.	15,000	64,043	—	79,043
Dr. Joachim Friedrich Kapp, M.D., Ph.D.	15,000	31,752	—	46,752
M. David MacFarlane, Ph.D.	15,000	47,702	—	62,702
Ley S. Smith	15,000	59,860	—	74,860
Konrad M. Weis, Ph.D.	12,500	56,068	—	68,568

- (1) Valuation based on the dollar amount of option grants recognized for financial statement reporting purposes pursuant to FAS 123(R) with respect to 2006. The assumptions we used with respect to the valuation of option grants are set forth in “Titan Pharmaceuticals Inc. Consolidated Financial Statements—Notes to Financial Statements—Note 1—Summary of Significant Accounting Policies—Stock-Based Compensation.” The aggregate option awards outstanding for each person in the table set forth above as of December 31, 2006 are as follows:

Name	Vested	Unvested	Exercise Price
Victor J. Bauer, Ph.D.	260,853	29,897	\$ 10.13
Eurelio M. Cavalier	138,853	41,147	\$ 8.02
Hubert Huckel, M.D.	161,853	46,147	\$ 9.87
Dr. Joachim Friedrich Kapp, M.D., Ph.D.	11,666	18,334	\$ 2.23
M. David MacFarlane, Ph.D.	57,603	32,397	\$ 2.61
Ley S. Smith	136,353	41,147	\$ 10.13
Konrad M. Weis, Ph.D.	120,228	42,397	\$ 9.99

The grant date fair values of option grants to our directors in 2006 are as follows:

Name	Options	Grant Date	Grant Date Fair Value (\$)
Victor J. Bauer, Ph.D.	5,000	1/3/2006	4,183
	20,000	8/29/2006	31,752
Eurelio M. Cavalier	5,000	1/3/2006	4,183
	20,000	8/29/2006	31,752
	15,000	9/5/2006	23,925
Hubert Huckel, M.D.	10,000	1/3/2006	8,366
	20,000	8/29/2006	31,752
	15,000	9/5/2006	23,925
Dr. Joachim Friedrich Kapp, M.D., Ph.D.	20,000	8/29/2006	31,752
M. David MacFarlane, Ph.D.	20,000	8/29/2006	31,752
	10,000	9/5/2006	15,950
Ley S. Smith	5,000	1/3/2006	4,183
	20,000	8/29/2006	31,752
	15,000	9/5/2006	23,925
Konrad M. Weis, Ph.D.	10,000	1/3/2006	8,366
	20,000	8/29/2006	31,752
	10,000	9/5/2006	15,950

Assumptions for calculating the grant date fair values are found under “Titan Pharmaceuticals Inc. Consolidated Financial Statements—Notes to Financial Statements—Note 1—Summary of Significant Accounting Policies—Stock-Based Compensation.”

## [Index to Financial Statements](#)

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

The following table sets forth, as of March 1, 2007, certain information concerning the beneficial ownership of our common stock by (i) each stockholder known by us to own beneficially five percent or more of our outstanding common stock; (ii) each director; (iii) each executive officer; and (iv) all of our executive officers and directors as a group, and their percentage ownership and voting power.

Name and Address of Beneficial Owner(1)	Shares Beneficially Owned(2)	Percent of Shares Beneficially Owned
Louis R. Bucalo, M.D.	2,275,129(3)	5.8%
Victor J. Bauer, Ph.D.	275,539(4)	*
Sunil Bhonsle	1,018,182(5)	2.6%
Eurelio M. Cavalier	179,893(6)	*
Robert E. Farrell, J.D.	474,318(7)	1.2%
Hubert Huckel, M.D.	242,061(8)	*
Dr. Joachim Friedrich Kapp, M.D., Ph.D.	13,333(9)	*
M. David MacFarlane, Ph.D.	73,852(10)	*
Ley S. Smith	157,393(11)	*
Konrad M. Weis, Ph.D.	191,426(12)	*
All executive officers and directors as a group (10) persons	4,901,366	12.6%

\* Less than one percent.

- (1) Unless otherwise indicated, the address of such individual is c/o Titan Pharmaceuticals, Inc., 400 Oyster Point Boulevard, Suite 505, South San Francisco, California 94080.
- (2) In computing the number of shares beneficially owned by a person and the percentage ownership of a person, shares of our common stock subject to options held by that person that are currently exercisable or exercisable within 60 days of March 1, 2007 are deemed outstanding. Such shares, however, are not deemed outstanding for purposes of computing the percentage ownership of each other person. Except as indicated in the footnotes to this table and pursuant to applicable community property laws, the persons named in the table have sole voting and investment power with respect to all shares of common stock.
- (3) Includes 1,775,129 shares issuable upon exercise of outstanding options.
- (4) Includes 266,895 shares issuable upon exercise of outstanding options.
- (5) Includes 897,888 shares issuable upon exercise of outstanding options.
- (6) Includes 149,893 shares issuable upon exercise of outstanding options.
- (7) Includes 404,238 shares issuable upon exercise of outstanding options.
- (8) Includes (i) 176,018 shares issuable upon exercise of outstanding options, (ii) 200 shares held by Dr. Huckel's son, and (iii) 3,643 shares held by his wife.
- (9) Includes 13,333 shares issuable upon exercise of outstanding options.
- (10) Includes 63,852 shares issuable upon exercise of outstanding options.
- (11) Includes 147,393 shares issuable upon exercise of outstanding options.
- (12) Includes 132,727 shares issuable upon exercise of outstanding options.

### Equity Compensation Plan Information

The following table sets forth aggregate information regarding our equity compensation plans in effect as of December 31, 2006:

Plan category	Number of securities to be issued upon exercise of outstanding options (a)	Weighted-average exercise price of outstanding options (b)	Number of securities remaining available for future issuance under equity compensation plans (c)
Equity compensation plans approved by security holders	4,883,804	\$ 6.80	1,279,496
Equity compensation plans not approved by security holders(1)(2)	1,706,406	\$ 8.03	434,688
<b>Total</b>	<b>6,590,210</b>	<b>\$ 7.12</b>	<b>1,714,184</b>

## Index to Financial Statements

- (1) In August 2002, we amended our 2001 Employee Non-Qualified Stock Option Plan. Pursuant to this amendment, a total of 1,750,000 shares of common stock were reserved and authorized for issuance for option grants to employees and consultants who are not officers or directors of Titan.
- (2) In November 1999 and in connection with the redemption of warrants, we granted 813,000 non-qualified stock options outside of our stock option plans to our executive officers, at an exercise price of \$12.69, vesting equally over 36 months from the date of grant.

For a discussion of our option plans, see “Item 11. Executive Compensation – Employee Benefit Plans.”

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

*Certain Relationships and Related Transactions.* None.

*Director Independence.* The following members of our Board of Directors meet the independence requirements and standards currently established by the American Stock Exchange: Victor J. Bauer, Eurilio M. Cavalier, Hubert E. Huckel, Joachim Friedrich Kapp, M. David MacFarlane, Ley S. Smith and Konrad M. Weis.

*Compensation Committee.* The Compensation Committee makes recommendations to the Board of Directors concerning salaries and incentive compensation for our officers, including our Chief Executive Officer, and employees and administers our stock option plans. The Compensation Committee consists of Eurilio M. Cavalier, Hubert E. Huckel and Konrad M. Weis, each of whom meets the independence requirements and standards currently established by the American Stock Exchange.

*Nominating Committee.* The purpose of the Nominating Committee is to assist the Board of Directors in identifying qualified individuals to become board members, in determining the composition of the Board of Directors and in monitoring the process to assess Board effectiveness. The Nominating Committee consists of Eurilio M. Cavalier, M. David MacFarlane and Ley S. Smith, each of whom meets the independence requirements and standards currently established by the American Stock Exchange.

*Audit Committee.* The Audit Committee (which is formed in compliance with Section 3(a)(58)(A) of the Securities Exchange Act of 1934) consists of Ley S. Smith, M. David MacFarlane and Hubert E. Huckel, each of whom meets the independence requirements and standards currently established by the American Stock Exchange and the SEC. In addition, the Board of Directors has determined that Mr. Ley Smith is an “audit committee financial expert” and “independent” as defined under the relevant rules of the SEC and the American Stock Exchange. The Audit Committee assists the Board by overseeing the performance of the independent auditors and the quality and integrity of Titan’s internal accounting, auditing and financial reporting practices. The Audit Committee is responsible for retaining (subject to stockholder ratification) and, as necessary, terminating, the independent auditors, annually reviews the qualifications, performance and independence of the independent auditors and the audit plan, fees and audit results, and pre-approves audit and non-audit services to be performed by the auditors and related fees.

### **Item 14. Principal Accountant Fees and Services.**

Aggregate fees billed by Odenberg, Ullakko, Muranishi & Co. LLP, an independent registered public accounting firm, during the fiscal years ended December 31, 2006 and 2005 were as follows:

	<u>2006</u>	<u>2005</u>
Audit Fees	\$211,600	\$191,126
Audit-Related Fees	3,000	11,315
Tax Fees	27,590	29,628
All Other Fees	—	—
Total	<u>\$242,190</u>	<u>\$232,069</u>

**Audit Fees**—This category includes aggregate fees billed by our independent auditors for the audit of Titan’s annual financial statements, audit of management’s assessment and effectiveness of internal controls over financial reporting, review of financial statements included in our quarterly reports on Form 10-Q and services that are normally provided by the auditor in connection with statutory and regulatory filings for those fiscal years.



---

## Index to Financial Statements

**Audit-Related Fees**—This category consists of services by our independent auditors that, including accounting consultations on transaction related matters, are reasonably related to the performance of the audit or review of Titan’s financial statements and are not reported above under Audit Fees.

**Tax Fees**—This category consists of professional services rendered for tax compliance and preparation of Titan’s corporate tax returns and other tax advice.

**All Other Fees**—During the years ended December 31, 2006 and 2005, Odenberg, Ullakko, Muranishi & Co. LLP did not incur any fees for other professional services.

The Audit Committee reviewed and approved all audit and non-audit services provided by Odenberg, Ullakko, Muranishi & Co. LLP and concluded that these services were compatible with maintaining its independence. The Audit Committee approved the provision of all non-audit services by Odenberg, Ullakko, Muranishi & Co. LLP.

### ***Pre-Approval Policies and Procedures***

In accordance with the SEC’s auditor independence rules, the Audit Committee has established the following policies and procedures by which it approves in advance any audit or permissible non-audit services to be provided to Titan by its independent auditor.

Prior to the engagement of the independent auditors for any fiscal year’s audit, management submits to the Audit Committee for approval lists of recurring audit, audit-related, tax and other services expected to be provided by the independent auditors during that fiscal year. The Audit Committee adopts pre-approval schedules describing the recurring services that it has pre-approved, and is informed on a timely basis, and in any event by the next scheduled meeting, of any such services rendered by the independent auditor and the related fees.

The fees for any services listed in a pre-approval schedule are budgeted, and the Audit Committee requires the independent auditor and management to report actual fees versus the budget periodically throughout the year. The Audit Committee will require additional pre-approval if circumstances arise where it becomes necessary to engage the independent auditor for additional services above the amount of fees originally pre-approved. Any audit or non-audit service not listed in a pre-approval schedule must be separately pre-approved by the Audit Committee on a case-by-case basis.

Every request to adopt or amend a pre-approval schedule or to provide services that are not listed in a pre-approval schedule must include a statement by the independent auditors as to whether, in their view, the request is consistent with the SEC’s rules on auditor independence.

The Audit Committee will not grant approval for:

- any services prohibited by applicable law or by any rule or regulation of the SEC or other regulatory body applicable to Titan;
- provision by the independent auditors to Titan of strategic consulting services of the type typically provided by management consulting firms; or
- the retention of the independent auditors in connection with a transaction initially recommended by the independent auditors, the tax treatment of which may not be clear under the Internal Revenue Code and related regulations and which it is reasonable to conclude will be subject to audit procedures during an audit of Titan’s financial statements.

Tax services proposed to be provided by the auditor to any director, officer or employee of Titan who is in an accounting role or financial reporting oversight role must be approved by the Audit Committee on a case-by-case basis where such services are to be paid for by Titan, and the Audit Committee will be informed of any services to be provided to such individuals that are not to be paid for by Titan.

In determining whether to grant pre-approval of any non-audit services in the “all other” category, the Audit Committee will consider all relevant facts and circumstances, including the following four basic guidelines:

- whether the service creates a mutual or conflicting interest between the auditor and the Company;
- whether the service places the auditor in the position of auditing his or her own work;
- whether the service results in the auditor acting as management or an employee of the Company; and
- whether the service places the auditor in a position of being an advocate for the Company.

**PART IV**

**Item 15. Exhibits and Financial Statements Schedules**

**(a) 1. Financial Statements**

An index to Consolidated Financial Statements appears on page F-1.

**2. Schedules**

All financial statement schedules are omitted because they are not applicable, not required under the instructions or all the information required is set forth in the financial statements or notes thereto.

**(b) Exhibits**

- 3.1 — Restated Certificate of Incorporation of the Registrant.(1)
- 3.2 — Form of Amendment to Restated Certificate of Incorporation of the Registrant.(1)
- 3.3 — By-laws of the Registrant.(1)
- 4.7 — Certificate of Designation of Series C Preferred Stock.(6)
- 4.8 — Registration Rights Agreement between the Registrant and Cornell Capital Partners, LP, dated September 28, 2005.(14)
- 10.1\* — 1993 Stock Option Plan.(1)
- 10.2\* — 1995 Stock Option Plan, as amended.(2)
- 10.3\* — Employment Agreement between the Registrant and Louis Bucalo dated February 1, 1993, amended as of February 3, 1994.(1)
- 10.4\* — Employment Agreement between Registrant and Richard Allen dated July 28, 1995.(1)
- 10.5\* — Employment Agreement between Registrant and Sunil Bhonsle, dated August 6, 1995.(1)
- 10.6 — Form of Indemnification Agreement.(1)
- †10.9 — MDR Exclusive License Agreement between Ingenex, Inc. (formerly Pharm-Gen Systems Ltd.) and the Board of Trustees of the University of Illinois dated May 6, 1992.(1)
- †10.11 — License Agreement between Theracell, Inc. and New York University dated November 20, 1992, as amended as of February 23, 1993 and as of February 25, 1995.(1)
- †10.12 — License Agreement between the Registrant and the Massachusetts Institute of Technology dated September 28, 1995.(1)
- †10.14 — Exclusive License Agreement between Ingenex, Inc. and the Board of Trustees of the University of Illinois, dated July 1, 1994.(1)
- †10.15 — Exclusive License Agreement between Ingenex, Inc. and the Board of Trustees of the University of Illinois, dated July 1, 1994.(1)
- †10.16 — License Agreement between Ingenex, Inc. and the Massachusetts Institute of Technology, dated September 11, 1992.(1)
- †10.17 — License Agreement between Ingenex, Inc. and Baylor College of Medicine, dated October 21, 1992.(1)
- 10.18 — Lease for Registrant's facilities, amended as of October 1, 2004.(13)
- †10.20 — License Agreement between Trilex Pharmaceuticals, Inc. (formerly Ascalon Pharmaceuticals, Inc.) and the University of Kentucky Research Foundation dated May 30, 1996.(3)
- †10.22 — License Agreement between the Registrant and Sanofi-Aventis SA (formerly Hoechst Marion Roussel, Inc.) effective as of December 31, 1996.(4)
- 10.23\* — Employment Agreement between Registrant and Robert E. Farrell dated August 9, 1996.(4)

---

## Index to Financial Statements

- †10.27 — License Agreement between the Registrant and Bar-Ilan Research and Development Company Limited effective November 25, 1997.(5)
- 10.28 — License Agreement between the Registrant and Ansan Pharmaceuticals, Inc. dated November 24, 1997.(5)
- †10.30 — Sublicense Agreement between the Registrant and Novartis Pharma AG dated November 20, 1997.(5)
- 10.31\* — 1998 Stock Option Plan, as amended.(7)
- †10.32 — License Agreement between the Registrant and Schering AG dated January 25, 2000.(8)
- 10.34 — Agreement and Plan of Merger by and among the Registrant, GeoMed Merger Sub Corp., GeoMed, Inc. and Dr. Lawrence Bernstein, Dr. Neil Gesundheit, Leland Wilson and Dr. Virgil Place dated July 11, 2000.(9)
- 10.35\* — 2001 Non-Qualified Employee Stock Option Plan.(10)
- 10.37\* — 2002 Stock Option Plan.(11)
- 10.38 — Merger Agreement between the Registrant and Developmental Therapeutics, Inc. dated October 15, 2003.(13)
- 10.39 — Addendums to License Agreement between the Registrant and Schering AG dated January 25, 2000.(13)
- 10.40\* — Amendment to Employment Agreement between the Registrant and Louis Bucalo dated February 7, 2005.(13)
- 10.41 — Standby Equity Distribution Agreement between the Registrant and Cornell Capital Partners, LP, dated September 28, 2005.(14)
- 14 — Code of Business Conduct and Ethics.(12)
- 21 — List of Subsidiaries.
- 23.1 — Consent of Odenberg, Ullakko, Muranishi & Co. LLP, Independent Registered Public Accounting Firm.
- 31.1 — Certification of Chief Executive Officer pursuant to Rule 13a-14(a) and Rule 15d-14(a) of the Securities Exchange Act, as amended.
- 31.2 — Certification of Chief Financial Officer pursuant to Rule 13a-14(a) and Rule 15d-14(a) of the Securities Exchange Act, as amended.
- 32 — Certification of Chief Executive Office and Chief Financial Officer pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

---

† Confidential treatment has been granted with respect to portions of this exhibit.

\* Represents a management contract or compensatory plan.

- (1) Incorporated by reference from the Registrant's Registration Statement on Form SB-2 (File No. 33-99386).
- (2) Incorporated by reference from the Registrant's Definitive Proxy Statement filed on September 3, 1996.
- (3) Incorporated by reference from the Registrant's Registration Statement on Form SB-2 (File No. 333-13469) filed on October 4, 1996, amended on November 25, 1996.
- (4) Incorporated by reference from the Registrant's Annual Report on Form 10-KSB for the year ended December 31, 1996.
- (5) Incorporated by reference from the Registrant's Registration Statement on Form S-3 (File No. 333-42367) filed on December 16, 1997.
- (6) Incorporated by reference from the Registrant's Annual Report on Form 10-K for the year ended December 31, 1997.
- (7) Incorporated by reference from the Registrant's Definitive Proxy Statement filed on July 28, 2000.
- (8) Incorporated by reference from the Registrant's Annual Report on Form 10-K for the year ended December 31, 1999.
- (9) Incorporated by reference from the Registrant's Quarterly Report on Form 10-Q for the period ended September 30, 2000.
- (10) Incorporated by reference from the Registrant's Annual Report on Form 10-K for the year ended December 31, 2001.
- (11) Incorporated by reference from the Registrant's Annual Report on Form 10-K for the year ended December 31, 2002.
- (12) Incorporated by reference from the Registrant's Annual Report on Form 10-K for the year ended December 31, 2003.
- (13) Incorporated by reference from the Registrant's Annual Report on Form 10-K for the year ended December 31, 2005.
- (14) Incorporated by reference from the Registrant's Current Report on Form 8-K dated September 28, 2005.



---

[Index to Financial Statements](#)

**TITAN PHARMACEUTICALS, INC.**

**INDEX TO CONSOLIDATED FINANCIAL STATEMENTS**

	<u>Page</u>
<a href="#">Reports of Independent Registered Public Accounting Firm</a>	F-2
<a href="#">Consolidated Balance Sheets</a>	F-4
<a href="#">Consolidated Statements of Operations</a>	F-5
<a href="#">Consolidated Statements of Stockholders' Equity</a>	F-6
<a href="#">Consolidated Statements of Cash Flows</a>	F-7
<a href="#">Notes to Consolidated Financial Statements</a>	F-8

**REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

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

We have audited management's assessment, included in the Management's Annual Report on Internal Control Over Financial Reporting included in Item 9A, that Titan Pharmaceuticals, Inc. and its subsidiaries (the "company") maintained effective internal control over financial reporting as of December 31, 2006, based on criteria established in *Internal Control—Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (the COSO criteria). The company's management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting. Our responsibility is to express an opinion on management's assessment and an opinion on the effectiveness of the company's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, evaluating management's assessment, testing and evaluating the design and operating effectiveness of internal control, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of the inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of the effectiveness to future periods are subject to the risk that the controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, management's assessment that the company maintained effective internal control over financial reporting as of December 31, 2006, is fairly stated, in all material respects, based on the COSO criteria. Also in our opinion, the company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2006, based on the COSO criteria.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets of Titan Pharmaceuticals, Inc. and its subsidiaries as of December 31, 2006 and 2005 and the related consolidated statements of operations, stockholders' equity, and cash flows for each of the three years in the period ended December 31, 2006, and our report dated February 27, 2007 expressed an unqualified opinion thereon.

/s/ Odenberg, Ullakko, Muranishi & Co. LLP

San Francisco, California  
February 27, 2007

**REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

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

We have audited the accompanying consolidated balance sheets of Titan Pharmaceuticals, Inc. and its subsidiaries as of December 31, 2006 and 2005, and the related consolidated statements of operations, stockholders' equity, and cash flows for each of the three years in the period ended December 31, 2006. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

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

In our opinion, the consolidated financial statements audited by us present fairly, in all material respects, the consolidated financial position of Titan Pharmaceuticals, Inc. and its subsidiaries at December 31, 2006 and 2005, and the consolidated results of their operations and their cash flows for each of the three years in the period ended December 31, 2006 in conformity with U.S. generally accepted accounting principles.

As discussed in Note 1 to the consolidated financial statements, the Company changed its method of accounting for share-based compensation in 2006 when it adopted SFAS No. 123R, "Share Based Payment" starting January 1, 2006.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the effectiveness of Titan Pharmaceuticals, Inc.'s internal control over financial reporting as of December 31, 2006, based on criteria established in *Internal Control—Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated February 27, 2007 expressed an unqualified opinion thereon.

/s/ Odenberg, Ullakko, Muranishi & Co. LLP

San Francisco, California  
February 27, 2007

**TITAN PHARMACEUTICALS, INC.**  
**CONSOLIDATED BALANCE SHEETS**

	December 31,	
	2006	2005
	(in thousands of dollars)	
<b>Assets</b>		
Current assets:		
Cash and cash equivalents	\$ 9,613	\$ 9,142
Marketable securities	4,102	8,227
Prepaid expenses, receivables and other current assets	504	1,216
Total current assets	<u>14,219</u>	<u>18,585</u>
Property and equipment, net	457	788
Investment in other companies	150	150
Other assets	214	214
	<u>\$ 15,040</u>	<u>\$ 19,737</u>
<b>Liabilities and Stockholders' Equity</b>		
Current liabilities:		
Accounts payable	\$ 561	\$ 518
Accrued clinical trials expenses	1,521	787
Other accrued liabilities	1,312	1,831
Total current liabilities	3,394	3,136
Commitments and contingencies		
Minority interest—Series B preferred stock of Ingenex, Inc.	<u>1,241</u>	<u>1,241</u>
Stockholders' Equity:		
Preferred stock, \$0.001 par value per share; 5,000,000 shares authorized, none issued and outstanding:	—	—
Common stock, at amounts paid in, \$0.001 par value per share; 75,000,000 shares authorized, 38,975,040 and 35,584,269 shares issued and outstanding at December 31, 2006 and 2005, respectively	224,221	214,331
Additional paid-in capital	10,118	9,264
Deferred compensation	—	(19)
Accumulated deficit	(223,944)	(208,207)
Accumulated other comprehensive income (loss)	10	(9)
Total stockholders' equity	<u>10,405</u>	<u>15,360</u>
	<u>\$ 15,040</u>	<u>\$ 19,737</u>

See accompanying notes.



**TITAN PHARMACEUTICALS, INC.**  
**CONSOLIDATED STATEMENTS OF OPERATIONS**

	Years ended December 31,		
	2006	2005	2004
	(in thousands, except per share amount)		
Revenue:			
License revenue	\$ 32	\$ 89	\$ 31
Operating expenses:			
Research and development	11,620	17,770	20,415
Acquired research and development	—	—	759
General and administrative	4,859	5,370	5,237
Total operating expenses	<u>16,479</u>	<u>23,140</u>	<u>26,411</u>
Loss from operations	(16,447)	(23,051)	(26,380)
Other income (expense):			
Interest income	717	570	673
Other income (expense)	(7)	19	(297)
Other income, net	710	589	376
Net loss	<u>\$ (15,737)</u>	<u>\$ (22,462)</u>	<u>\$ (26,004)</u>
Basic and diluted net loss per share	<u>\$ (0.42)</u>	<u>\$ (0.69)</u>	<u>\$ (0.83)</u>
Weighted average shares used in computing basic and diluted net loss per share	<u>37,902</u>	<u>32,635</u>	<u>31,381</u>

See accompanying notes.

TITAN PHARMACEUTICALS, INC

CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY

(in thousands)

	Preferred Stock		Common Stock		Additional Paid-In Capital	Deferred Compensation	Accumulated Deficit	Accumulated Other Comprehensive Income (Loss)	Total Stockholders' Equity
	Shares	Amount	Shares	Amount					
<b>Balances at December 31, 2003</b>	<b>222</b>	<b>\$ —</b>	<b>28,903</b>	<b>\$195,331</b>	<b>\$ 9,047</b>	<b>\$ (211)</b>	<b>\$ (159,741)</b>	<b>\$ —</b>	<b>\$ 44,426</b>
Comprehensive loss:									
Net loss							(26,004)		(26,004)
Unrealized loss on marketable securities							(51)		(51)
Comprehensive loss									(26,055)
Issuance of common stock, net of issuance costs of \$1,020			3,075	14,355					14,355
Issuance of common stock upon exercise of options			180	211					211
Issuance of common stock upon tender of Proneura, Inc. shares			150	367					367
Compensation related to stock options					280	(154)			126
Amortization of deferred compensation						283			283
<b>Balances at December 31, 2004</b>	<b>222</b>	<b>—</b>	<b>32,308</b>	<b>210,264</b>	<b>9,327</b>	<b>(82)</b>	<b>(185,745)</b>	<b>(51)</b>	<b>33,713</b>
Comprehensive loss:									
Net loss							(22,462)		(22,462)
Unrealized gain on marketable securities							42		42
Comprehensive loss									(22,420)
Issuance of common stock, net of issuance costs of \$263			3,131	3,887					3,887
Issuance of common stock upon exercise of options			145	180					180
Compensation related to stock options					(63)				(63)
Amortization of deferred compensation						63			63
Redemption of series C preferred stock	(222)								
<b>Balances at December 31, 2005</b>	<b>—</b>	<b>\$ —</b>	<b>35,584</b>	<b>\$214,331</b>	<b>\$ 9,264</b>	<b>\$ (19)</b>	<b>\$ (208,207)</b>	<b>\$ (9)</b>	<b>\$ 15,360</b>
Comprehensive loss:									
Net loss							(15,737)		(15,737)
Unrealized gain on marketable securities							19		19
Comprehensive loss									(15,718)
Issuance of common stock, net of issuance costs of \$730			3,077	9,270					9,270
Issuance of common stock upon exercise of options			314	620					620
Compensation related to stock options					854				854
Amortization of deferred compensation						19			19
<b>Balances at December 31, 2006</b>	<b>—</b>	<b>\$ —</b>	<b>38,975</b>	<b>\$224,221</b>	<b>\$ 10,118</b>	<b>\$ —</b>	<b>\$ (223,944)</b>	<b>\$ 10</b>	<b>\$ 10,405</b>

See accompanying notes.

TITAN PHARMACEUTICALS, INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS

	Years ended December 31,		
	2006	2005	2004
	(in thousands of dollars)		
<b>Cash flows from operating activities:</b>			
Net loss	\$(15,737)	\$(22,462)	\$(26,004)
Adjustments to reconcile net loss to net cash used in operating activities:			
Depreciation and amortization	389	405	466
(Gain) loss on investment activities	—	(8)	261
Loss on disposition of property and equipment	5	—	4
Acquired research and development	—	—	759
Non-cash compensation related to stock options	873	—	409
Changes in operating assets and liabilities:			
Prepaid expenses, receivables and other current assets	712	(320)	254
Accounts payable	42	(171)	(816)
Accrued clinical trials and other liabilities	216	(365)	755
Net cash used in operating activities	<u>(13,500)</u>	<u>(22,921)</u>	<u>(23,912)</u>
<b>Cash flows from investing activities:</b>			
Purchases of property and equipment, net	(63)	(149)	(725)
Purchases of marketable securities	(15,596)	(7,202)	(12,098)
Proceeds from maturities of marketable securities	19,740	29,884	20,800
Net cash provided by investing activities	<u>4,081</u>	<u>22,533</u>	<u>7,977</u>
<b>Cash flows from financing activities:</b>			
Issuance of common stock, net	9,890	4,067	14,566
Net cash provided by financing activities	<u>9,890</u>	<u>4,067</u>	<u>14,566</u>
<b>Net increase (decrease) in cash and cash equivalents</b>	471	3,679	(1,369)
Cash and cash equivalents at beginning of year	<u>9,142</u>	<u>5,463</u>	<u>6,832</u>
<b>Cash and cash equivalents at end of year</b>	9,613	9,142	5,463
Marketable securities at end of year	<u>4,102</u>	<u>8,227</u>	<u>30,859</u>
<b>Cash, cash equivalents and marketable securities at end of year</b>	<u>\$ 13,715</u>	<u>\$ 17,369</u>	<u>\$ 36,322</u>
<i>Schedule of non-cash transaction:</i>			
Issuance of common stock to acquire technologies, net	\$ —	\$ —	\$ 367

See accompanying notes.

**TITAN PHARMACEUTICALS, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**1. Organization and Summary of Significant Accounting Policies**

***The Company and its Subsidiaries***

We are a biopharmaceutical company developing proprietary therapeutics for the treatment of central nervous system (CNS) disorders, cardiovascular disease, bone disease and other disorders. Our product development programs focus primarily on large pharmaceutical markets with significant unmet medical needs and commercial potential. We are directly developing our product candidates and also utilizing strategic partnerships, including a collaboration with Bayer Schering Pharma AG, Germany (Bayer Schering). These collaborations help fund product development and enable us to retain significant economic interest in our products. At December 31, 2006, we owned 81% of Ingenex, Inc. assuming the conversion of all preferred stock to common stock. In the fourth quarter of 2004, we completed the merger of ProNeura, Inc., our 89% owned subsidiary, into Titan. We operate in only one business segment, the development of pharmaceutical products.

We expect to continue to incur substantial additional operating losses from costs related to continuation of product and technology development, clinical trials, and administrative activities. We believe that with our current cash balances and the Standby Equity Distribution agreement we will have access to sufficient working capital to sustain our planned operations through the end of 2007.

Although the Standby Equity Distribution agreement provides us with up to an additional \$31.0 million of financing, subject to the receipt of required shareholder approval, we will need to seek additional financing sources to fund our product development activities, and will be required to obtain substantial funding to commercialize any products other than iloperidone or Spheramine that we may successfully develop. If we are unable to complete a debt or equity offering, or otherwise obtain sufficient financing when and if needed, we may be required to reduce, defer or discontinue one or more of our product development programs.

***Basis of Presentation and Consolidation***

The accompanying consolidated financial statements include the accounts of Titan and our wholly and majority owned subsidiaries. All significant intercompany balances and transactions are eliminated.

***Use of Estimates***

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

***Stock Option Plans***

Effective January 1, 2006, we adopted SFAS 123R – “Share Based Payment” (SFAS 123R) using the modified-prospective-transition method. Under this transition method, stock compensation cost recognized beginning January 1, 2006 includes: (a) compensation cost for all share-based payments granted prior to, but not yet vested as of January 1, 2006, based on the grant-date fair value estimated in accordance with the original provisions of SFAS 123, and (b) compensation cost for all share-based payments granted on or subsequent to January 1, 2006, based on the grant-date fair value estimated in accordance with the provisions of SFAS 123R. Results for prior periods have not been restated.

We use the Black-Scholes-Merton option-pricing model with the following assumptions to estimate the share-based compensation expense for the year ended December 31, 2006: 1) weighted-average risk-free interest rate of 4.8%; 2) no expected dividend payments; 3) expected holding period of 5.8 years based on the simplified method provided in Staff Accounting Bulletin No. 107 for “plain vanilla options”; 4) weighted-average volatility factor of 0.64 based on historical stock prices; and 5) an estimated forfeiture rate of 2% of options granted to management and 31% of options granted to non-management based on historical data.

The SFAS 123R share-based compensation expense recorded for awards under the stock option plans was approximately \$873,000, net of estimated forfeitures, during the year ended December 31, 2006. The share-based compensation expense of \$354,000 was recorded in research and development expense and \$519,000 was recorded in general and administrative expense during the twelve month period ended December 31, 2006. No tax benefit was recognized related to share-based compensation expense since we have incurred operating losses and we have established a full valuation allowance to offset all the potential tax benefits associated with our deferred tax assets. Our basic and diluted loss per share for the year ended December 31, 2006 increased by \$0.03, due to adopting SFAS 123R.

During the year ended December 31, 2006 we granted 1,157,650 options to employees, directors and consultants to purchase common stocks. The following table summarizes option activity for the year ended December 31, 2006:

## Index to Financial Statements

<i>(in thousands, except per share amounts)</i>	Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term	Aggregate Intrinsic Value
Outstanding at January 1, 2006	6,499	\$ 7.56		
Granted	1,158	1.69		
Exercised	(314)	1.98		
Cancelled	(753)	4.68		
Outstanding at December 31, 2006	<u>6,590</u>	<u>\$ 7.12</u>	<u>5.24</u>	<u>\$ 3,606</u>
Options exercisable at December 31, 2006	5,282	\$ 8.41	4.33	\$ 1,752

As of December 31, 2006 there was approximately \$778,000 of total unrecognized compensation expense related to non-vested stock options. This expense is expected to be recognized over a weighted-average period of 0.59 year.

Until December 31, 2005, we elected to follow Accounting Principles Board Opinion No. 25 (APB 25), "Accounting for Stock Issued to Employees," rather than the alternative method of accounting prescribed by SFAS 123, "Accounting for Stock-Based Compensation." Under APB 25, no compensation expense is recognized when the exercise price of our employee stock options equals the market price of the underlying stock on the date of grant. The following table illustrates the effect on our net loss and net loss per share if we had applied the provisions of SFAS 123 to estimate and recognize compensation expense for our share-based employee compensation during the year ended December 31, 2005 and 2004.

	Years Ended December 31,	
	2005	2004
Net loss, as reported	\$ (22,462)	\$ (26,004)
Add: Stock-based employee compensation expense included in reported net loss	(27)	268
Deduct: Stock-based employee compensation expense determined under fair value method for all stock option grants	(873)	(1,390)
Pro forma net loss	<u>\$ (23,362)</u>	<u>\$ (27,126)</u>
Basic and diluted net loss per share, as reported	<u>\$ (0.69)</u>	<u>\$ (0.83)</u>
Pro forma basic and diluted net loss per share	<u>\$ (0.72)</u>	<u>\$ (0.86)</u>

The fair value of options was estimated at the date of grant using a Black-Scholes-Merton option-pricing model with the following assumptions for the year ended December 31, 2005 and 2004, respectively: weighted-average volatility factor of 0.70 and 0.70; no expected dividend payments; weighted-average risk-free interest rate in effect of 4.1% and 3.0%; and a weighted-average expected life of 3.12 and 3.97 years. In the pro forma information for periods prior to 2006, we accounted for forfeitures as they occurred.

### ***Cash, Cash Equivalents and Marketable Securities***

Our cash and investment policy emphasizes liquidity and preservation of principal over other portfolio considerations. We select investments that maximize interest income to the extent possible given these two constraints. We satisfy liquidity requirements by investing excess cash in securities with different maturities to match projected cash needs and limit concentration of credit risk by diversifying our investments among a variety of high credit-quality issuers and limit the amount of credit exposure to any one issuer. The estimated fair values have been determined using available market information. We do not use derivative financial instruments in our investment portfolio.

All investments with original maturities of three months or less are considered to be cash equivalents. Our marketable securities, consisting primarily of high-grade debt securities including money market funds, U.S. government and corporate notes and bonds, and commercial paper, are classified as available-for-sale at time of purchase and carried at fair value. If the fair value of a security is below its amortized cost for six consecutive months or if its decline is due to a significant adverse event, the impairment is considered to be other-than-temporary. Other-than-temporary declines in fair value of our marketable securities are charged against interest income. We recognized expenses of approximately \$27,000 in 2006, \$45,000 in 2005, and \$102,000 in 2004 as a result of charges related to other-than-temporary declines in the fair values of certain of our marketable securities. Amortization of premiums and discounts, and realized gains and losses are included in interest income. Unrealized gains and losses are included as accumulated other comprehensive income (loss), a separate component of stockholders' equity. The cost of securities sold is based on use of the specific identification method.

### ***Property and Equipment***

Property and equipment are recorded at cost and depreciated using the straight-line method over the estimated useful lives of the assets ranging from three to five years. Leasehold improvements are amortized over the shorter of the lease term or the estimated useful life of the assets.

### ***Investment in Other Companies***

We have invested in equity instruments of privately held companies for business and strategic purposes. These investments are classified as long-term assets and are accounted for under the cost method as we do not have the ability to exercise significant influence over their operations. We monitor our investments for impairment and record reductions in carrying value when events or changes in circumstances indicate that the carrying value may not be recoverable. Determination of impairment is based on a number of factors, including an assessment of the strength of investee's management, the length of time and extent to which the fair value has been less than our cost basis, the financial condition and near-term prospects of the investee, fundamental changes to the business prospects of the investee, share prices of subsequent offerings, and our intent and ability to hold the investment for a period of time sufficient to allow for any anticipated recovery in our carrying value.

In December 2001, we made a \$300,000 equity investment in Molecular Medicine BioServices, Inc. for 714,286 shares of Series A Preferred stock, and at December 31, 2006, these shares represent 3.7% of total equity in the company. In September 2004, we recorded a \$150,000 reduction in the carrying value of our investment in Molecular Medicine BioServices, Inc., and included the loss in other income (expense).

### ***Revenue Recognition***

We generate revenue principally from collaborative research and development arrangements, technology licenses, and government grants. Revenue arrangements with multiple components are divided into separate units of accounting if certain criteria are met, including whether the delivered component has stand-alone value to the customer, and whether there is objective and reliable evidence of the fair value of the undelivered items. Consideration received is allocated among the separate units of accounting based on their respective fair values, and the applicable revenue recognition criteria are then applied to each of the units.

Revenue is recognized when the four basic criteria of revenue recognition are met: (1) a contractual agreement exists; (2) transfer of technology has been completed or services have been rendered; (3) the fee is fixed or determinable; and (4) collectibility is reasonably assured. For each source of revenue, we comply with the above revenue recognition criteria in the following manner:

- Collaborative arrangements typically consist of non-refundable and/or exclusive technology access fees, cost reimbursements for specific research and development spending, and various milestone and future product royalty payments. If the delivered technology does not have stand-alone value or if we do not have objective or reliable evidence of the fair value of the undelivered component, the amount of revenue allocable to the delivered technology is deferred. Non-refundable upfront fees with stand-alone value that are not dependent on future performance under these agreements are recognized as revenue when received, and are deferred if we have continuing performance obligations and have no evidence of fair value of those obligations. Cost reimbursements for research and development spending are recognized when the related costs are incurred and when collections are reasonably expected. Payments received related to substantive, performance-based "at-risk" milestones are recognized as revenue upon achievement of the clinical success or regulatory event specified in the underlying contracts, which represent the culmination of the earnings process. Amounts received in advance are recorded as deferred revenue until the technology is transferred, costs are incurred, or a milestone is reached.
- Technology license agreements typically consist of non-refundable upfront license fees, annual minimum access fees or royalty payments. Non-refundable upfront license fees and annual minimum payments received with separable stand-alone values are recognized when the technology is transferred or accessed, provided that the technology transferred or accessed is not dependent on the outcome of our continuing research and development efforts.
- Government grants, which support our research efforts in specific projects, generally provide for reimbursement of approved costs as defined in the notices of grants. Grant revenue is recognized when associated project costs are incurred.

### ***Research and Development Costs***

Research and development expenses include internal and external costs. Internal costs include salaries and employment related expenses, facility costs, administrative expenses and allocations of corporate costs. External expenses consist of costs associated with outsourced clinical research organization activities, sponsored research studies, product registration, patent application and prosecution, and investigator sponsored trials. In accordance with SFAS No. 2, “*Accounting for Research and Development Costs*,” all such costs are charged to expense as incurred.

### ***Net Loss Per Share***

We calculate basic net loss per share using the weighted average common shares outstanding for the period. Diluted net income per share would include the impact of other dilutive equity instruments, primarily our preferred stock, options and warrants. For the years ended December 31, 2006, 2005, and 2004, outstanding preferred stock, options and warrants totaled 6.6 million, 6.7 million, and 6.7 million shares, respectively. We reported net losses for all years presented and, therefore, preferred stock, options and warrants were excluded from the calculation of diluted net loss per share as they were anti-dilutive.

### ***Comprehensive Income (Loss)***

Comprehensive income (loss) is comprised of net loss and other comprehensive income. The only component of other comprehensive income is unrealized gains and losses on our marketable securities. Comprehensive loss for the years ended December 31, 2006, 2005, and 2004 was \$15.7 million, \$22.4 million, and \$26.1 million, respectively. Comprehensive income (loss) has been disclosed in the Consolidated Statements of Stockholders’ Equity for all periods presented.

### ***Recent Accounting Pronouncements***

In December 2004, the Financial Accounting Standards Board (FASB) issued their final standard on accounting for share-based payments in FASB Standard No. 123R (revised 2004), *Share-Based Payment* (SFAS 123R). This statement replaces FASB Statement 123, *Accounting for Stock-Based Compensation* (SFAS 123), and supersedes Accounting Principles Board (APB) Opinion No. 25, *Accounting for Stock Issued to Employees*. The statement is effective for all interim and annual periods beginning after December 15, 2005 and requires companies to measure and recognize compensation expense for all share-based payments at fair value in the consolidated statement of income.

Effective January 1, 2006, we adopted SFAS 123R using the modified-prospective-transition method. Under this transition method, stock compensation cost recognized beginning January 1, 2006 includes: (a) compensation cost for all share-based payments granted prior to, but not yet vested as of January 1, 2006, based on the grant-date fair value estimated in accordance with the original provisions of SFAS 123, and (b) compensation cost for all share-based payments granted on or subsequent to January 1, 2006, based on the grant-date fair value estimated in accordance with the provisions of SFAS 123R. Results for prior periods have not been restated.

In June 2006, the FASB issued Interpretation No. 48, “Accounting for Uncertainty in Income Taxes—an interpretation of FASB Statement No. 109” (“FIN 48”). This Interpretation clarifies the accounting for uncertainty in income taxes recognized in a company’s financial statements in accordance with FASB Statement No. 109, *Accounting for Income Taxes*. FIN 48 prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. This Interpretation also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure, and transition. The evaluation of a tax position in accordance with FIN 48 is a two-step process. The first step is recognition: The Company determines whether it is “more-likely-than-not” that a tax position will be sustained upon examination, including resolution of any related appeals or litigation processes, based on the technical merits of the position. In evaluating whether a tax position has met the “more-likely-than-not” recognition threshold, the company presumes that the position will be examined by the appropriate taxing authority that would have full knowledge of all relevant information. The second step is measurement: A tax position that meets the “more-likely-than-not” recognition threshold is measured to determine the amount of benefit to recognize in the financial statements. The tax position is measured at the largest amount of benefit that is greater than 50 percent likely to be realized upon ultimate settlement. FIN 48 is effective for fiscal years beginning after December 15, 2006. The Company has not yet determined what impact this statement will have on its results of operations or financial position.

[Index to Financial Statements](#)

**2. Cash, Cash Equivalents and Marketable Securities**

The following is a summary of our cash, cash equivalents and marketable securities at December 31, 2006 and 2005 (in thousands):

Classified as:	2006				2005			
	Amortized Cost	Gross Unrealized Gain	Gross Unrealized (Loss)	Fair Value	Amortized Cost	Gross Unrealized Gain	Gross Unrealized (Loss)	Fair Value
Cash	\$ 2,053	\$ —	\$ —	\$ 2,053	\$ 1,444	\$ —	\$ —	\$ 1,444
Cash equivalents:								
Money market funds	7,560	—	—	7,560	7,698	—	—	7,698
Total cash and cash equivalents	9,613	—	—	9,613	9,142	—	—	9,142
Marketable securities:								
Securities of the U.S. government and its agencies	4,092	10	—	4,102	8,235	9	(17)	8,227
Total cash, cash equivalents and marketable securities	\$ 13,705	\$ 10	\$ —	\$ 13,715	\$ 17,377	\$ 9	\$ (17)	\$ 17,369
<b>Securities available-for-sale:</b>								
Maturing within 1 year	\$ 3,392			\$ 3,400	\$ 7,236			\$ 7,237
Maturing between 1 to 2 years	\$ 700			\$ 702	\$ 999			\$ 990

There were no material gross realized gains or losses on sales of marketable securities for the years ended December 31, 2006, 2005 and 2004.

**3. Property and Equipment**

Property and equipment consisted of the following at December 31 (in thousands):

	2006	2005
Furniture and office equipment	\$ 579	\$ 565
Leasehold improvements	459	459
Laboratory equipment	852	964
Computer equipment	977	920
	2,866	2,908
Less accumulated depreciation and amortization	(2,409)	(2,120)
Property and equipment, net	\$ 457	\$ 788

Depreciation and amortization expense was \$389,000, \$405,000, and \$466,000 for the years ended December 31, 2006, 2005, and 2004, respectively.

**4. Research and License Agreements**

We have entered into various agreements with research institutions, universities, clinical research organizations and other entities for the performance of research and development activities and for the acquisition of licenses related to those activities. Expenses under these agreements totaled approximately \$690,000, \$700,000, and \$3.5 million in the years ended December 31, 2006, 2005, and 2004, respectively.

At December 31, 2006, the annual aggregate commitments we have under these agreements, including minimum license payments, are as follows (in thousands):

2007	\$133
2008	102
2009	136
2010	136
2011	136
	<u>\$643</u>



---

## [Index to Financial Statements](#)

After 2011, we must make annual payments aggregating \$136,000 per year to maintain certain licenses. Certain licenses provide for the payment of royalties by us on future product sales, if any. In addition, in order to maintain these licenses and other rights during product development, we must comply with various conditions including the payment of patent related costs and obtaining additional equity investments.

### **5. Agreement with Sanofi-Aventis SA**

In 1997, we entered into an exclusive license agreement with Sanofi-Aventis SA (formerly Hoechst Marion Roussel, Inc.). The agreement gave us a worldwide license to the patent rights and know-how related to the antipsychotic agent iloperidone, including the ability to develop, use, sublicense, manufacture and sell products and processes claimed in the patent rights. We are required to make additional benchmark payments as specific milestones are met. Upon commercialization of the product, the license agreement provides that we will pay royalties based on net sales.

### **6. Iloperidone Sublicense to Novartis Pharma AG**

We entered into an agreement with Novartis Pharma AG (Novartis) in 1997 pursuant to which we granted Novartis a sublicense for the worldwide (with the exception of Japan) development, manufacturing and marketing of iloperidone. In April 2001, we entered into an amendment to the agreement for the development and commercialization of iloperidone in Japan. Under the amendment, in exchange for rights to iloperidone in Japan, we received a \$2.5 million license fee in May 2001. Novartis will make our milestone payments to Sanofi-Aventis during the life of the Novartis agreement, and will also pay to Sanofi-Aventis and us a royalty on future net sales of the product, providing us with a net royalty of 8% on the first \$200 million of sales annually and 10% on all sales above \$200 million on an annual basis. Novartis has assumed the responsibility for all clinical development, registration, manufacturing and marketing of iloperidone, and we have no remaining obligations under the terms of this agreement, except for maintaining certain usual and customary requirements, such as confidentiality covenants.

In June 2004, we announced that Vanda Pharmaceuticals, Inc. (Vanda) had acquired from Novartis the worldwide rights to develop and commercialize iloperidone, our proprietary antipsychotic agent in Phase III clinical development for the treatment of schizophrenia and related psychotic disorders. Under its agreement with Novartis, Vanda is pursuing advancement of the iloperidone Phase III development program. All of our rights and economic interests in iloperidone, including royalties on sales of iloperidone, remain essentially unchanged under the agreement.

### **7. Licensing and Collaborative Agreement with Bayer Schering Pharma AG**

In January 2000, we entered into a licensing and collaborative agreement with Bayer Schering Pharma AG (Bayer Schering), under which we will collaborate with Bayer Schering on manufacturing and clinical development of our cell therapy product, Spheramine®, for the treatment of Parkinson's disease. Under the agreement, we will perform clinical development activities for which we will receive funding. As of December 31, 2006, we have recognized \$2.8 million under this agreement. In February 2002, we announced that we received a \$2.0 million milestone payment from Bayer Schering. The milestone payment followed Bayer Schering's decision in the first quarter 2002 to initiate larger, randomized clinical testing of Spheramine for the treatment of patients with advanced Parkinson's disease following the successful completion of our Phase I/II clinical study of Spheramine. As a result, we recognized \$2.0 million in contract revenue in the first quarter of 2002. Bayer Schering will fully fund, and manage in collaboration with us, all future pilot and pivotal clinical studies, and manufacturing and development activities. We are entitled to receive up to an aggregate of \$8 million over the life of the Bayer Schering agreement upon the achievement of specific milestones. We will also receive a royalty on future net sales of the product.

## 8. DITPA Acquisition

On October 16, 2003, we announced the acquisition of a novel product in clinical testing for the treatment of congestive heart failure (CHF). The product in development, 3,5-diiodothyropropionic acid (DITPA), is an orally active analogue of thyroid hormone that has demonstrated in preclinical and clinical studies to date the ability to improve cardiac function, with no significant adverse effects. We acquired DITPA through the acquisition of Developmental Therapeutics, Inc. (DTI), a private company established to develop DITPA, and the exclusive licensee of recently issued U.S. patent and pending U.S. and international patent applications covering DITPA. We acquired DTI in a stock transaction for 1,187,500 shares of our common stock valued at approximately \$3.6 million using the average market price of our common stock over the five-day trading period, including and prior to the date of the merger in accordance with generally accepted accounting principles. We also made a cash payment of \$171,250 to the licensor of the technology. In the fourth quarter of 2003, the total acquisition cost of \$3.9 million was reported as acquired research and development in the consolidated statement of operations. An additional payment of 712,500 shares of our common stock will be made only upon the achievement of positive pivotal study results or certain other substantial milestones within five years. In addition, a cash payment of \$102,750 or, alternatively, an additional payment of 37,500 shares of our common stock, will be made to the licensor of the technology upon achievement of such study results or such other substantial milestones within five years. No specific milestones have been achieved related to this acquisition as of December 31, 2006. In October 2006, we discontinued further enrollment in our Phase II study of DITPA in CHF. We will subsequently analyze data collected to date. In addition to the discontinuation of our Phase II clinical study in CHF, the Department of Veteran's Affairs has indicated that it will discontinue its Cooperative Studies Program Phase II study of DITPA in CHF patients.

## 9. Commitments and Contingencies

### *Lease Commitments*

We lease facilities under operating leases that expire at various dates through June 2010. We also lease certain office equipment under operating and capital leases that expire at various dates through July 2009. Rental expense was \$703,000, \$721,000, and \$832,000 for years ended December 31, 2006, 2005, and 2004, respectively.

The following is a schedule of future minimum lease payments at December 31, 2006 (in thousands):

2007	\$ 636
2008	587
2009	584
2010	296
Thereafter	—
	<u>\$2,103</u>

### *Legal Proceedings*

In March 2005, Dr. Bernard Sabel initiated an appraisal proceeding in the Court of Chancery of the State of Delaware relating to the merger of our subsidiary ProNeura, Inc. into Titan. The complaint indicates that Mr. Sabel wants the court to appraise the value of the 108,800 shares of the common stock of ProNeura owned by him. The complaint does not specify an amount that Mr. Sabel considers the fair value of the shares. Discovery is proceeding in connection with this appraisal proceeding.

## 10. Guarantees and Indemnifications

As permitted under Delaware law and in accordance with our Bylaws, we indemnify our officers and directors for certain events or occurrences while the officer or director is or was serving at the Company's request in such capacity. The term of the indemnification period is for the officer's or director's lifetime. The maximum amount of potential future indemnification is unlimited; however, we have a director and officer insurance policy that limits our exposure and may enable us to recover a portion of any future amounts paid. We believe the fair value of these indemnification agreements is minimal. Accordingly, we have not recorded any liabilities for these agreements as of December 31, 2006.

In the normal course of business, we have commitments to make certain milestone payments to various clinical research organizations in connection with our clinical trial activities. Payments are contingent upon the achievement of specific milestones or events as defined in the agreements, and we have made appropriate accruals in our consolidated financial statements for those milestones that were achieved as of December 31, 2006. We also provide indemnifications of varying scope to our clinical research organizations and investigators against claims made by third parties arising from the

---

## [Index to Financial Statements](#)

use of our products and processes in clinical trials. Historically, costs related to these indemnification provisions were immaterial. We also maintain various liability insurance policies that limit our exposure. We are unable to estimate the maximum potential impact of these indemnification provisions on our future results of operations.

### 11. Stockholders' Equity

#### *Preferred Stock*

In connection with the merger of our Trilex Pharmaceuticals, Inc. subsidiary (Trilex) in 1997, we issued 222,400 shares of Series C convertible preferred stock (the Series C Preferred) to certain members of the Trilex management team and to certain consultants of Trilex. The Series C Preferred automatically converts to our common stock, on a one-to-one basis, only if certain development milestones are achieved within a certain timeframe. Upon achievement of the milestones, we would be required to value the technology using the then fair market value of our common stock issuable upon conversion. Certain milestones were not achieved by October 6, 2004. In February 2005, we redeemed all of the outstanding shares of Series C Preferred Stock at a redemption price equal to the aggregate par value of the shares plus accrued and unpaid dividends, if any. There were no accrued and unpaid dividends outstanding at the time of the redemption.

#### *Common Stock*

On September 28, 2005, we entered into a Standby Equity Distribution Agreement with Cornell Capital Partners. Under the agreement, we can require Cornell to purchase up to \$35.0 million of our common stock over a two year period following the effective date of a registration statement covering the shares of the common stock to be sold to Cornell Capital Partners. We can make draw-downs under the agreement in \$2.0 million increments. At the closing of each draw-down (which will take place six days after our notification to Cornell Capital Partners) we will issue to Cornell Capital Partners a number of shares of our common stock equal to the amount of the draw-down divided by the lowest daily volume weighted average price of our common stock during the five trading days following the draw-down notice to Cornell Capital Partners. At each closing, we will pay 5% of the amount of the draw-down to Cornell Capital Partners and \$500 to Yorkville Associates Management, the investment advisor to Cornell Capital Partners. We are not obligated to make any draw-downs under the agreement, and will not pay any additional fees to Cornell Capital Partners if we do not do so. We paid Cornell Capital Partners a one-time commitment fee equal to \$140,000 in the form of 75,407 shares of common stock, Monitor Capital, Inc., a placement agent fee equal to \$10,000 in the form of 5,386 shares of common stock and paid Yorkville Advisors Management a structuring fee of \$10,000, all of which are underwriting discounts payable or paid to Cornell Capital Partners. As of December 31, 2006, we had completed a total of five draw-downs under the Standby Equity Distribution Agreement selling a total of 3,050,435 shares of our common stock for gross proceeds of approximately \$4.0 million. Net proceeds were approximately \$3.8 million.

We can issue 3,344,059 additional shares under the agreement without receipt of the required shareholders' approval. We did not make any draw-downs under this facility in 2006.

In October 2004, we issued 149,599 shares of our common stock in exchange for 101,700 shares of ProNeura, Inc. (ProNeura) common stock under a share exchange agreement with two of the three minority shareholders of ProNeura. Our common stock was valued at \$367,000 using the average market price of our common stock over a five day trading period, including two days prior to and subsequent to the date of issuance.

In February 2004, we filed a shelf registration statement with the Securities and Exchange Commission to sell up to \$50 million of common or preferred stock. Under this registration statement, shares may be sold periodically to provide additional funds for our operations. In March 2004, we completed a sale of 3,075,000 shares of our common stock offered under the registration statement at a price of \$5.00 per share, for gross proceeds of approximately \$15.4 million. Net proceeds were approximately \$14.4 million. In March 2006, we completed a sale of 3,076,924 shares of our common stock offered under the registration statement at a price of \$3.25 per share, for gross proceeds of approximately \$10 million. Net proceeds were approximately \$9.3 million. This registration statement expired in February 2007.

In February 2007, we filed a shelf registration statement with the Securities and Exchange Commission to sell up to \$50 million of common or preferred stock. Under this registration statement, shares may be sold periodically to provide additional funds for our operations.

#### *Shares Reserved for Future Issuance*

As of December 31, 2006, shares of common stock reserved by us for future issuance consisted of the following (shares in thousands):

Stock options	6,590
DTI merger contingent shares	750
	<u>7,340</u>

## 12. Stock Option Plans

In October 2005, we repriced 223,134 non-executive employee options previously granted under the 1998 Stock Option Plan. The weighted average original exercise price of the repriced options was \$23.89. The exercise price of the new options is \$5.00.

In August 2005, we adopted an amendment to the 2002 Stock Option Plan (2002 Plan) to (i) permit the issuance of Shares of restricted stock and stock appreciation rights to participants under the 2002 Plan, and (ii) increase the number of Shares issuable pursuant to grants under the 2002 Plan from 2,000,000 to 3,000,000.

In July 2002, we adopted the 2002 Stock Option Plan (2002 Plan). The 2002 Plan assumed the options which remain available for grant under our option plans previously approved by stockholders. Under the 2002 Plan and predecessor plans, a total of 6.4 million shares of our common stock were authorized for issuance to employees, officers, directors, consultants, and advisers. Options granted under the 2002 Plan and predecessor plans may either be incentive stock options within the meaning of Section 422 of the Internal Revenue Code and/or options that do not qualify as incentive stock options; however, only employees are eligible to receive incentive stock options. Options granted under the option plans generally expire no later than ten years from the date of grant, except when the grantee is a 10% shareholder, in which case the maximum term is five years from the date of grant. Options generally vest at the rate of one fourth after one year from the date of grant and the remainder ratably over the subsequent three years, although options with different vesting terms are granted from time-to-time. Generally, the exercise price of any options granted under the 2002 Plan must be at least 100% of the fair market value of our common stock on the date of grant, except when the grantee is a 10% shareholder, in which case the exercise price shall be at least 110% of the fair market value of our common stock on the date of grant.

In July 2002, our Board of Directors elected to continue the option grant practice under our amended 1998 Option Plan, which provided for the automatic grant of non-qualified stock options (Directors' Options) to our directors who are not 10% stockholders (Eligible Directors). Each Eligible Director will be granted an option to purchase 10,000 shares of common stock on the date that such person is first elected or appointed a director. Commencing on the day immediately following the later of (i) the 2000 annual stockholders meeting, or (ii) the first annual meeting of stockholders after their election to the Board, each Eligible Director will receive an automatic biennial (i.e. every two years) grant of an option to purchase 15,000 shares of common stock as long as such director is a member of the Board of Directors. In addition, each Eligible Director will receive an automatic annual grant of an option to purchase 5,000 shares of common stock for each committee of the Board on which they serve. The exercise price of the Director's Options shall be equal to the fair market value of our common stock on the date of grant. Commencing in 2005, the biennial grant of options to non-employee directors pursuant to our stockholder-approved stock option plans was increased from 15,000 options to 20,000 options.

In August 2001, we adopted the 2001 Employee Non-Qualified Stock Option Plan (2001 NQ Plan) pursuant to which 1,750,000 shares of common stock were authorized for issuance for option grants to employees and consultants who are not officers or directors of Titan. Options granted under the option plans generally expire no later than ten years from the date of grant. Option vesting schedule and exercise price are determined at time of grant by the Board of Directors. Historically, the exercise prices of options granted under the 2001 NQ Plan were 100% of the fair market value of our common stock on the date of grant.

Activity under our stock option plans, as well as non-plan activity are summarized below (shares in thousands):

	Shares Available For Grant	Number of Options Outstanding	Weighted Average Exercise Price
Balance at December 31, 2003	2,138	5,952	\$ 9.39
Options granted	(1,407)	1,407	\$ 2.90
Options exercised	—	(180)	\$ 1.17
Options cancelled	734	(734)	\$ 7.81
Balance at December 31, 2004	1,465	6,445	\$ 8.39
Increase in shares reserved	1,000	—	—
Options granted	(953)	953	\$ 3.03
Options exercised	—	(145)	\$ 1.24
Options cancelled	754	(754)	\$ 10.14
Balance at December 31, 2005	2,266	6,499	\$ 7.56
Options granted	(1,158)	1,158	\$ 1.69
Options exercised	—	(314)	\$ 1.98
Options cancelled	606	(753)	\$ 4.68
Balance at December 31, 2006	1,714	6,590	\$ 7.12

## [Index to Financial Statements](#)

Our option plans allow for stock options issued as the result of a merger or consolidation of another entity, including the acquisition of minority interest of our subsidiaries, to be added to the maximum number of shares provided for in the plan (Substitute Options). Consequently, Substitute Options are not returned to the shares reserved under the plan when cancelled. During 2006, 2005 and 2004, the number of Substitute Options cancelled was immaterial.

Options for 5.3 million and 5.6 million shares were exercisable at December 31, 2006 and 2005, respectively. The options outstanding at December 31, 2006 have been segregated into four ranges for additional disclosure as follows (option shares in thousands):

Range of Exercise Prices	Options Outstanding			Options Exercisable	
	Number Outstanding	Weighted Average Remaining Life (Years)	Weighted Average Exercise Price	Number Exercisable	Weighted Average Exercise Price
\$0.08 - \$2.35	1,705	7.81	\$ 1.64	769	\$ 1.65
\$2.36 - \$3.69	1,668	6.29	\$ 2.98	1,296	\$ 3.09
\$3.77 - \$11.63	2,005	3.41	\$ 8.02	2,004	\$ 8.02
\$12.68 - \$43.63	1,212	3.21	\$ 19.03	1,213	\$ 19.03
\$0.08 - \$43.63	6,590	5.24	\$ 7.12	5,282	\$ 8.41

In addition, Ingenex has a stock option plan under which options to purchase common stock of Ingenex have been and may be granted. No options have been granted under such plan since 1997.

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

Based upon the above methodology, the weighted-average fair value of options granted during the years ended December 31, 2006, 2005, and 2004 was \$1.06, \$1.00, and \$1.65, respectively. A tabular presentation of pro forma net loss and net loss per share information for all reporting periods is presented in Note 1.

### 13. Minority Interest

The \$1.2 million received by Ingenex upon the issuance of its Series B convertible preferred stock has been classified as minority interest in the consolidated balance sheets. As a result of the Series B preferred stockholders' liquidation preference, the balance has not been reduced by any portion of the losses of Ingenex.

Amounts invested by outside investors in the common stock of the consolidated subsidiaries have been apportioned between minority interest and additional paid-in capital in the consolidated balance sheets. Losses applicable to the minority interest holdings of the subsidiaries' common stock have been reduced to zero.

### 14. Income Taxes

As of December 31, 2006, we had net operating loss carryforwards for federal income tax purposes of approximately \$222.2 million that expire at various dates through 2026, and federal research and development tax credits of approximately \$6.5 million that expire at various dates through 2026. We also had net operating loss carryforwards for state income tax purposes of approximately \$87.6 million that expire at various dates through 2016, and state research and development tax credits of approximately \$5.4 million which do not expire.

Current federal and California tax laws include substantial restrictions on the utilization of net operating losses and tax credits in the event of an ownership change of a corporation. Accordingly, the Company's ability to utilize net operating loss and tax credit carryforwards may be limited as a result of such ownership changes. Such a limitation could result in the expiration of carryforwards before they are utilized.

Deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. Significant components of our deferred tax assets are as follows (in thousands):

[Index to Financial Statements](#)

	December 31,	
	2006	2005
Deferred tax assets:		
Net operating loss carryforwards	\$ 75,769	\$ 73,974
Research credit carryforwards	10,048	9,112
Other, net	5,902	5,975
Total deferred tax assets	91,719	89,061
Valuation allowance	(91,719)	(89,061)
Net deferred tax assets	\$ —	\$ —

Realization of deferred tax assets is dependent upon future earnings, if any, the timing and amount of which are uncertain. Accordingly, the net deferred tax assets have been fully offset by a valuation allowance. The valuation allowance increased by \$2.7 million, \$11.9 million, and \$7.6 million during 2006, 2005, and 2004, respectively.

Under SFAS 123R, the deferred tax asset for Net Operating Losses as of December 31, 2006 excludes deductions for excess tax benefits related to stock based compensation. The deferred tax asset pertaining to Net Operating Losses decreased approximately \$4.2M.

In November 2005, the FASB issued Financial Statement Position (“FSP”) on SFAS No. 123(R)-3, *Transition Election Related to Accounting for Tax Effects of Share-Based Payment Awards*. Effective upon issuance, FSP No. 123(R)-3 provides for an alternative transition method for calculating the tax effects of stock-based compensation expense pursuant to SFAS No. 123(R). The alternative transition method provides simplified approaches to establish the beginning balance of a tax benefit pool comprised of the additional paid-in capital (“APIC”) related to the tax effects of employee stock-based compensation expense, and to determine the subsequent impact on the APIC tax benefit pool and the statement of cash flows of stock-based awards that were outstanding upon the adoption of SFAS No. 123(R). The Company has made the election to calculate the tax effects of stock-based compensation expense using the alternative transition method pursuant to FSP No. 123(R)-3 and computed the beginning balance of the APIC tax benefit pool by applying the simplified method. Based on the Company’s historical losses, the Company did not have cumulative excess tax benefits from stock-based compensation available in APIC that could be used to offset an equal amount of future tax shortfalls (i.e., when the amount of the tax deductible stock-based compensation is less than the related stock-based compensation cost).

The provision for income taxes consists of state minimum taxes due. The effective tax rate of the Company’s provision (benefit) for income taxes differs from the federal statutory rate as follows (in thousands):

	Year Ending December 31,	
	2006	2005
Computed at 34%	\$(5,348)	\$(7,637)
State Taxes	(909)	(1,301)
Book losses not currently benefited	6,219	8,926
Other	47	18
Total	\$ 9	\$ 6

---

[Index to Financial Statements](#)

**15. Quarterly Financial Data (Unaudited)**

	<u>First</u>	<u>Second</u>	<u>Third</u>	<u>Fourth</u>
	<u>Quarter</u>	<u>Quarter</u>	<u>Quarter</u>	<u>Quarter</u>
	(in thousands, except per share amount)			
<b>2006</b>				
Total revenue	\$ 1	1	1	\$ 29
Net loss	\$(4,705)	\$(3,426)	\$(4,340)	\$(3,266)
Basic and diluted net loss per share	\$ (0.13)	\$ (0.09)	\$ (0.11)	\$ (0.09)
<b>2005</b>				
Total revenue	\$ 14	13	1	\$ 61
Net loss	\$(6,296)	\$(5,742)	\$(6,378)	\$(4,046)
Basic and diluted net loss per share	\$ (0.19)	\$ (0.18)	\$ (0.20)	\$ (0.12)

**List of Subsidiaries**

<u>Subsidiary*</u>	<u>Jurisdiction of Incorporation</u>	<u>Name Under which Subsidiary does Business</u>
Ingenex, Inc.	Delaware	This subsidiary is currently inactive
Developmental Therapeutics, Inc.	Delaware	Developmental Therapeutics

\* We own 100% of the outstanding common stock of Developmental Therapeutics, Inc. and 81% of the outstanding common stock of Ingenex, Inc.



**CONSENT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

We consent to the incorporation by reference in the Registration Statements on Forms S-8 (No. 333-42533, No. 333-86001, No. 333-62734, No. 333-100011 and No. 333-138673, pertaining to the 1995 Stock Option Plan, the 1998 Stock Option Plan, as amended and restated, and the 2002 Stock Option Plan, as amended), Forms S-3 (No. 333-33710, No. 333-51250, No. 333-53538 and No. 333-140518) and Form S-1 No. 333-129086 of Titan Pharmaceuticals, Inc. of our reports dated February 27, 2007, relating to the consolidated financial statements of Titan Pharmaceuticals, Inc., Titan Pharmaceuticals, Inc. management's assessment of the effectiveness of internal control over financial reporting, and the effectiveness of internal control over financial reporting of Titan Pharmaceuticals, Inc., included in this Annual Report on Form 10-K for the year ended December 31, 2006.

/s/ ODENBERG ULLAKKO MURANISHI & CO. LLP

San Francisco, California

March 2, 2007

## CERTIFICATION PURSUANT TO RULE 13a-14(A) OF THE EXCHANGE ACT

I, Louis R. Bucalo, M.D., Chairman, President and Chief Executive Officer of Titan Pharmaceuticals, Inc., certify that:

1. I have reviewed this annual report on Form 10-K of Titan Pharmaceuticals, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation;
  - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: March 5, 2007

/s/ LOUIS R. BUCALO

Louis R. Bucalo, M.D.

*Chairman, President and Chief Executive Officer*

## CERTIFICATION PURSUANT TO RULE 13a-14(A) OF THE EXCHANGE ACT

I, Robert E. Farrell, J.D., Executive Vice President and Chief Financial Officer of Titan Pharmaceuticals, Inc., certify that:

1. I have reviewed this annual report on Form 10-K of Titan Pharmaceuticals, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation;
  - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: March 5, 2007

/s/ ROBERT E. FARRELL

Robert E. Farrell, J.D.

*Executive Vice President and Chief Financial Officer*

## CERTIFICATIONS PURSUANT TO 18 U.S.C. SECTION 1350

In connection with the Annual Report of Titan Pharmaceuticals, Inc. (the "Company") on Form 10-K for the period ended December 31, 2006 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Louis R. Bucalo, M.D., Chairman, President and Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. section 1350, as adopted pursuant to section 906 of the Sarbanes-Oxley Act of 2002, that, to the best of my knowledge:

(1) The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

(2) The information contained in the Report fairly presents, in all material respects, the financial condition and result of operations of the Company for the period certified.

Signed at the City of South San Francisco, in the State of California, this 5<sup>th</sup> day of March 2007.

/s/ LOUIS R. BUCALO

Louis R. Bucalo, M.D.

In connection with the Annual Report of Titan Pharmaceuticals, Inc. (the "Company") on Form 10-K for the period ended December 31, 2006 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Robert E. Farrell, J.D., Executive Vice President and Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. section 1350, as adopted pursuant to section 906 of the Sarbanes-Oxley Act of 2002, that, to the best of my knowledge:

(1) The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

(2) The information contained in the Report fairly presents, in all material respects, the financial condition and result of operations of the Company for the period certified.

Signed at the City of South San Francisco, in the State of California, this 5<sup>th</sup> day of March 2007.

/s/ ROBERT E. FARRELL

Robert E. Farrell, J.D.