

MANHATTAN PHARMACEUTICALS INC  
Form 10-Q  
November 14, 2011

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, DC 20549

FORM 10-Q

x QUARTERLY REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended September 30, 2011

OR

.. TRANSITION REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission file number 001-32639

Manhattan Pharmaceuticals, Inc.  
(Exact Name of Registrant as Specified in Its Charter)

Delaware  
(State or other jurisdiction of  
incorporation or organization)

36-3898269  
(I.R.S. Employer Identification No.)

48 Wall Street, New York, New York 10005  
(Address of principal executive offices)

(212) 582-3950  
(Issuer's telephone number)

Check whether the issuer: (1) 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 issuer was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes x No ..

Indicate by check mark whether the registrant has submitted and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes x No ..

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

Large accelerated filer .. Accelerated filer .. Non-accelerated filer .. Smaller reporting company x

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

Yes .. No x

As of November 2, 2011 there were 7,398,316 shares of the issuer's common stock, \$.001 par value, outstanding.

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### Forward-Looking Statements

This quarterly report on Form 10-Q contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, or the Securities Act, and Section 21E of the Securities and Exchange Act of 1934. Any statements about our expectations, beliefs, plans, objectives, assumptions or future events or performance are not historical facts and may be forward-looking. These statements are often, but not always, made through the use of words or phrases such as “anticipate,” “estimate,” “plan,” “project,” “expect,” “may,” “intend” and similar words or phrases. Accordingly, these statements involve estimates, assumptions and uncertainties that could cause actual results to differ materially from those expressed in them. These statements are therefore subject to risks and uncertainties, known and unknown, which could cause actual results and developments to differ materially from those expressed or implied in such statements. Such risks and uncertainties relate to, among other factors:

- the development of our drug candidates;
- the regulatory approval of our drug candidates;
- our use of clinical research centers and other contractors;
- our ability to find collaborative partners for research, development and commercialization of potential products;
- acceptance of our products by doctors, patients or payers;
- our ability to market any of our products;
- our history of operating losses;
- our ability to compete against other companies and research institutions;
- our ability to secure adequate protection for our intellectual property;
- our ability to attract and retain key personnel;
- availability of reimbursement for our product candidates;
- the effect of potential strategic transactions on our business;
- our ability to obtain adequate financing; and
- the volatility of our stock price.

Further, any forward-looking statement speaks only as of the date on which it is made, and we undertake no obligation to update any forward-looking statement or statements to reflect events or circumstances after the date on which such statement is made or to reflect the occurrence of unanticipated events. New factors emerge from time to time, and it is not possible for us to predict which factors will arise. In addition, we cannot assess the impact of each factor on our business or the extent to which any factor, or combination of factors, may cause actual results to differ materially from those contained in any forward-looking statements.

## Part I – Financial Information

## Item 1. Unaudited Condensed Consolidated Financial Statements

MANHATTAN PHARMACEUTICALS, INC. and SUBSIDIARY  
(A Development Stage Company)  
Condensed Consolidated Balance Sheets

	September 30, 2011 (unaudited)	December 31, 2010 (See Note 1)
<b>Assets</b>		
<b>Current assets:</b>		
Cash and cash equivalents	\$ 212,280	\$ 478,668
Grant receivable	-	244,479
Debt issue costs	-	4,408
Other current assets	100,759	141,622
<b>Total current assets</b>	<b>313,039</b>	<b>869,177</b>
In-process research and development	17,742,110	17,742,110
Property and equipment, net	1,580	2,984
Other assets	7,750	21,370
<b>Total assets</b>	<b>\$ 18,064,479</b>	<b>\$ 18,635,641</b>
<b>Liabilities and Stockholders' Deficiency</b>		
<b>Current Liabilities:</b>		
Notes payable, current portion, net of discount	\$ 761,314	\$ 2,054,246
Accounts payable and accrued expenses	167,719	223,516
Interest payable, current portion, net of beneficial conversion	47,223	480,890
Derivative liability	538,830	534,846
<b>Total current liabilities</b>	<b>1,515,086</b>	<b>3,293,498</b>
Notes payable, noncurrent portion, net of discount	16,388,797	16,130,571
Interest payable, noncurrent portion	455,214	626,697
Exchange obligation	-	3,949,176
<b>Total liabilities</b>	<b>18,359,097</b>	<b>23,999,942</b>
<b>Commitments and contingencies</b>		
<b>Stockholders' deficiency:</b>		
Preferred stock, \$.001 par value. Authorized 1,500,000 shares; no shares issued and outstanding at September 30, 2011 and December 31, 2010	-	-
Common stock, \$.001 par value. Authorized 500,000,000 shares; 7,398,316 shares issued and outstanding at September 30, 2011 and 2,419,305 shares issued and outstanding at December 31, 2010	7,398	2,419
Contingently issuable shares	15,890	15,890
Additional paid-in capital	60,693,779	55,927,180
Deficit accumulated during the development stage	(61,011,685 )	(61,309,790 )
<b>Total stockholders' deficiency</b>	<b>(294,618 )</b>	<b>(5,364,301 )</b>

Total liabilities and stockholders' deficiency	\$ 18,064,479	\$ 18,635,641
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See accompanying notes to unaudited condensed consolidated financial statements.

MANHATTAN PHARMACEUTICALS, INC. and SUBSIDIARY  
(A Development Stage Company)  
Condensed Consolidated Statements of Operations  
(unaudited)

	Three months ended September 30,		Nine months ended September 30,		Cumulative period from August 6, 2001 (inception) to September 30, 2011
	2011	2010	2011	2010	2011
Revenue	\$-	\$-	\$-	\$-	\$ -
<b>Costs and expenses:</b>					
Research and development	95,897	236,734	541,292	305,500	29,369,296
General and administrative	165,946	278,897	609,542	1,264,666	20,323,939
In-process research and development charge	-	-	-	-	11,887,807
Impairment of intangible assets	-	-	-	-	1,248,230
Loss on disposition of intangible assets	-	-	-	-	1,213,878
Total operating expenses	261,843	515,631	1,150,834	1,570,166	64,043,150
Operating loss	(261,843 )	(515,631 )	(1,150,834 )	(1,570,166 )	(64,043,150 )
<b>Other (income) expense:</b>					
Equity in losses of Hedrin JV	-	-	-	-	750,000
Change in fair value of derivative liability	(2,100,898 )	(830,165 )	(39,587 )	(2,696,900 )	(2,455,261 )
Interest and other income	(196 )	(76,275 )	(4,518,150 )	(228,305 )	(7,610,133 )
Interest expense	1,165,078	349,562	1,882,886	937,555	3,795,334
Loss on early extinguishment of debt	1,225,912	-	1,225,912	159,070	1,384,982
Realized gain on sale of marketable equity securities	-	-	-	-	(76,032 )
Total other (income) expense	289,896	(556,878 )	(1,448,939 )	(1,828,580 )	(4,211,110 )
Net income (loss)	(551,739 )	41,247	298,105	258,414	(59,832,040 )
Preferred stock dividends (including imputed amounts)	-	-	-	-	(1,179,645 )
Net income (loss) applicable to common shares	\$(551,739 )	\$41,247	\$298,105	\$258,414	\$(61,011,685 )
<b>Net income (loss) per common share:</b>					
Basic and diluted	\$(0.16 )	\$0.02	\$0.10	\$0.12	
<b>Weighted average shares of common stock outstanding:</b>					
Basic and diluted	3,431,031	2,419,305	2,861,792	2,176,257	

See accompanying notes to condensed consolidated financial statements.



MANHATTAN PHARMACEUTICALS, INC. and SUBSIDIARY  
(A Development Stage Company)  
Condensed Consolidated Statements of Stockholders' Equity (Deficiency)  
(unaudited)

	Common stock shares	Common stock amount	Additional paid- in capital	Deficit accumulated during development stage	Other	Total stockholders' equity (deficiency)
Stock issued at \$0.02 per share for subscription receivable	203,355	\$ 203	\$ 3,797	\$-	\$(4,000 )	\$(0 )
Net loss	-	-	-	(56,796 )	-	(56,796 )
Balance at December 31, 2001	203,355	203	3,797	(56,796 )	(4,000 )	(56,796 )
Proceeds from subscription receivable	-	-	-	-	4,000	4,000
Stock issued at \$0.02 per share for license rights	50,839	51	949	-	-	1,000
Stock options issued for consulting services	-	-	60,589	-	(60,589 )	-
Common stock issued at \$31.50 per share, net of expenses	60,866	61	1,704,257	-	-	1,704,318
Amortization of unearned consulting services	-	-	-	-	22,721	22,721
Net loss	-	-	-	(1,037,320 )	-	(1,037,320 )
Balance at December 31, 2002	315,060	315	1,769,592	(1,094,116 )	(37,868 )	637,923
Common stock issued at \$31.50 per share, net of expenses	26,436	26	743,665	-	-	743,691
Effect of reverse acquisition	125,752	126	2,336,115	-	-	2,336,241
Payment for fraction shares for stock combination	-	-	(300 )	-	-	(300 )
Preferred stock issued at \$10 per share, net of expenses	-	-	9,045,176	-	1,000	9,046,176
Imputed preferred stock dividend	-	-	418,182	(418,182 )	-	-
Amortization of unearned consulting services	-	-	-	-	37,868	37,868
Unrealized loss on short-term investments	-	-	-	-	(7,760 )	(7,760 )

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Net loss	-	-	-	(5,960,907 )	-	(5,960,907 )
Balance at December 31, 2003	467,248	467	14,312,430	(7,473,205 )	(6,760 )	6,832,932
Exercise of stock options	552	1	30,099	-	-	30,100
Common stock issued at \$55.00 per share, net of expenses	67,379	67	3,361,651	-	-	3,361,718
Preferred stock dividend accrued	-	-	-	(585,799 )	-	(585,799 )
Preferred stock dividend paid by issuance of preferred shares	-	-	281,073	-	25	281,098
Conversion of preferred stock to common stock at \$55.00 per share	31,005	31	140	-	(171 )	-
Warrants issued for consulting services	-	-	125,558	-	(120,968 )	4,590
Amortization of unearned consulting services	-	-	-	-	100,800	100,800
Unrealized gain and reversal of unrealized loss on short-term investments	-	-	-	-	20,997	20,997
Net loss	-	-	-	(5,896,031 )	-	(5,896,031 )
Balance at December 31, 2004	566,184	566	18,110,951	(13,955,035 )	(6,077 )	4,150,405
Common stock issued at \$55.50 and \$57.50 per share, net of expenses	238,354	238	12,249,971	-	-	12,250,209
Common stock issued at \$55.50 in satisfaction of accounts payable	13,513	13	749,987	-	-	750,000
Exercise of stock options	648	1	32,399	-	-	32,400
Exercise of warrants	5,597	6	68,485	-	-	68,491
Preferred stock dividend accrued	-	-	-	(175,663 )	-	(175,663 )
Preferred stock dividend paid by issuance of preferred shares	-	-	477,736	-	42	477,778
Conversion of preferred stock to common stock at \$55.00 per share	162,937	163	733	-	(896 )	-
Stock issued in connection with acquisition of Tarpan Therapeutics, Inc.	214,621	215	11,052,769	-	-	11,052,984
Reversal of unrealized gain on short-term investments	-	-	-	-	(12,250 )	(12,250 )
	-	-	66,971	-	20,168	87,139

Share-based compensation						
Net loss	-	-	-	(19,140,997)	-	(19,140,997)
Balance at December 31, 2005	1,201,854	1,202	42,810,002	(33,271,695)	987	9,540,496
Cashless exercise of warrants	547	-	-	-	-	-
Costs associated with private placement	-	-	(15,257 )	-	-	(15,257 )
Unrealized loss on short-term investments	-	-	-	-	(987 )	(987 )
Share-based compensation						
Net loss	-	-	1,675,499	-	-	1,675,499
Net loss	-	-	-	(9,695,123 )	-	(9,695,123 )
Balance at December 31, 2006	1,202,401	1,202	44,470,244	(42,966,818)	-	1,504,628

MANHATTAN PHARMACEUTICALS, INC. and SUBSIDIARY  
(A Development Stage Company)  
Condensed Consolidated Statements of Stockholders' Equity (Deficiency)  
(unaudited)

	Common stock shares	Common stock amount	Additional paid- in capital	Deficit accumulated during development stage	Other	Total stockholders' equity (deficiency)
Common stock issued at \$42.00 and \$45.00 per share, net of expenses	203,710	\$ 204	\$ 7,851,981	\$-	\$-	\$7,852,185
Common stock issued at \$36.00 per share in satisfaction of accounts payable	556	1	19,999	-	-	20,000
Common stock issued with in-licensing agreement at \$45.00 per share	2,500	2	112,498	-	-	112,500
Common stock issued with in-licensing agreement at \$40.00 per share	3,000	3	119,997	-	-	120,000
Warrants issued for consulting services	-	-	83,670	-	-	83,670
Exercise of warrants	206	-	7,233	-	-	7,233
Cashless exercise of warrants	112	-	(6 )	-	-	(6 )
Share-based compensation	-	-	1,440,956	-	-	1,440,956
Net loss	-	-	-	(12,032,252)	-	(12,032,252)
Balance at December 31, 2007	1,412,485	1,412	54,106,572	(54,999,070)	-	(891,086 )
Sale of warrant	-	-	150,000	-	-	150,000
Warrants issued with 12% notes	-	-	170,128	-	-	170,128
Share-based compensation	-	-	463,890	-	-	463,890
Net loss	-	-	-	(4,268,858 )	-	(4,268,858 )
Balance at December 31, 2008	1,412,485	1,412	54,890,590	(59,267,928)	-	(4,375,926 )
Cumulative effect of a change in accounting principle	-	-	(150,000 )	127,778	-	(22,222 )
Balance at January 1, 2009, as adjusted	1,412,485	1,412	54,740,590	(59,140,150)	-	(4,398,148 )
	-	-	53,044	-	-	53,044

Warrants issued with secured 12% notes						
Share-based compensation	-	-	353,438	-	-	353,438
Net loss	-	-	-	(2,793,285 )	-	(2,793,285 )
Balance at December 31, 2009	1,412,485	1,412	55,147,072	(61,933,435)	-	(6,784,951 )
Common stock issued at \$3.50 per share, net of expenses	865,572	866	2,584,621	-	-	2,585,487
Derivative liability associated with warrants issued with common stock	-	-	(3,497,898 )	-	-	(3,497,898 )
Shares issued and issuable in Merger with Ariston	141,248	141	1,475,906	-	15,890	1,491,937
Share-based compensation	-	-	217,479	-	-	217,479
Net income	-	-	-	623,645	-	623,645
Balance at December 31, 2010	2,419,305	2,419	55,927,180	(61,309,790)	15,890	(5,364,301 )
Share-based compensation	-	-	19,210	-	-	19,210
Shares issued on achievement of Ariston milestone	176,561	177	220,524	-	-	220,701
Roundup adjustment for 1 for 50 reverse stock split	251	-	-	-	-	-
Derivative liability associated with warrant amendment	-	-	(115,000 )	-	-	(115,000 )
Beneficial conversion feature of Secured 12% Notes Payable and interest	-	-	2,245,596	-	-	2,245,596
Conversion of Secured 12% Notes Payable and interest into common stock (see Note 1)	4,802,199	4,802	2,396,269	-	-	2,401,071
Net income	-	-	-	298,105	-	298,105
Balance at September 30, 2011	7,398,316	\$ 7,398	\$ 60,693,779	\$(61,011,685)	\$ 15,890	\$(294,618 )

See accompanying notes to unaudited condensed consolidated financial statements.

MANHATTAN PHARMACEUTICALS, INC. and SUBSIDIARY  
(A Development Stage Company)  
Condensed Consolidated Statements of Cash Flows  
(unaudited)

	Nine months ended 2011	September 30, 2010	Cumulative period from August 6, 2001 (inception) to September 30, 2011
<b>Cash flows from operating activities:</b>			
Net income/(loss)	\$ 298,105	\$ 258,414	\$ (59,832,040 )
Adjustments to reconcile net income/(loss) to net cash used in operating activities:			
Equity in losses of Hedrin JV	-	-	750,000
Non cash gain on Nordic settlement	(4,017,488 )	-	(4,017,488 )
Share-based compensation	19,210	211,771	4,419,000
Amortization of OID, issue costs and beneficial conversion feature	1,041,745	288,772	1,978,376
Change in fair value of derivative liability	(39,587 )	(2,696,900 )	(3,131,569 )
Loss on early extinguishment of debt	1,225,912	159,070	1,384,982
Shares issued in connection with in-licensing agreement	-	-	232,500
Shares issued in connection with Ariston milestone	220,701	-	220,701
Warrants issued to consultant	-	-	83,670
Amortization of intangible assets	-	-	145,162
Gain on sale of marketable equity securities	-	-	(76,032 )
Depreciation	1,404	2,644	232,267
Noncash portion of in-process research and development charge	-	-	11,721,623
Loss on impairment and disposition of intangible assets	-	-	2,462,108
Other	-	-	23,917
Changes in operating assets and liabilities, net of acquisitions:			
Decrease in grant receivable	244,479	-	-
Decrease in prepaid expenses and other current assets	40,508	60,612	77,999
Decrease/(increase) in other assets	10,859	-	(25,511 )
Decrease in accounts payable and accrued expenses	(55,797 )	(332,972 )	(178,104 )
Increase in interest payable	843,561	620,219	1,722,574
Net cash used in operating activities	(166,388 )	(1,428,370 )	(41,805,865 )
<b>Cash flows from investing activities:</b>			
Purchase of property and equipment	-	(2,844 )	(242,452 )
Cash acquired in connection with acquisitions	-	519,365	493,334
Net cash provided from the purchase and sale of short-term investments	-	-	435,938
Proceeds from sale of license	-	-	200,001
Net cash provided by investing activities	-	516,521	886,821
<b>Cash flows from financing activities:</b>			
Proceeds related to sale of common stock, net	-	2,163,486	28,059,748
Proceeds from sale of preferred stock, net	-	-	9,046,176
Proceeds from the Hedrin JV agreement	-	-	3,199,176

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Proceeds from sale of notes payable	-	-	1,509,915
Sale of warrant	-	-	150,000
Net repayments of notes payable	(100,000 )	(193,667 )	(1,207,124 )
Other, net	-	-	373,433
Net cash provided by/(used in) financing activities	(100,000 )	1,969,819	41,131,324
Net increase (decrease) in cash and cash equivalents	(266,388 )	1,057,970	212,280
Cash and cash equivalents at beginning of period	478,668	17,996	-
Cash and cash equivalents at end of period	\$ 212,280	\$ 1,075,966	\$ 212,280

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MANHATTAN PHARMACEUTICALS, INC. and SUBSIDIARY  
(A Development Stage Company)  
Condensed Consolidated Statements of Cash Flows  
(unaudited)

	Nine months ended September 30,		Cumulative period from August 6, 2001 (inception) to September 30, 2011
	2011	2010	
<b>Supplemental disclosure of cash flow information:</b>			
Interest paid	\$ 882	\$ 28,212	\$ 68,387
<b>Supplemental disclosure of noncash investing and financing activities:</b>			
Issuance of common stock for acquisitions	\$ -	\$ 1,491,937	\$ 14,881,163
Conversion of debt to common stock and warrants	2,401,071	422,000	2,823,071
In-process research and development acquired	-	17,742,110	17,742,110
Investment in Hedrin JV	-	500,000	1,250,000
Beneficial conversion feature	2,245,596	-	2,245,596
Warrants issued with notes payable	-	-	250,562
Note issued to settle accrued expenses	-	-	211,900
Common stock issued in satisfaction of accounts payable	-	-	770,000
Imputed and accrued preferred stock dividend	-	-	1,179,644
Conversion of preferred stock to common stock	-	-	1,067
Preferred stock dividends paid by issuance of shares	-	-	759,134
Issuance of common stock in connection with in-licensing agreement	-	-	232,500
Marketable equity securities received in connection with sale of license	-	-	359,907
Warrants issued to consultant	-	-	83,670
Net liabilities assumed over assets acquired in business combination	-	-	(675,416 )
Cashless exercise of warrants	-	-	33

See accompanying notes to unaudited condensed consolidated financial statements.



MANHATTAN PHARMACEUTICALS, INC. and SUBSIDIARY  
(a Development Stage Company)  
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation

The accompanying unaudited condensed consolidated financial statements of Manhattan Pharmaceuticals, Inc. ("Manhattan") and subsidiary (the "Company") have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information and the rules and regulations of the Securities and Exchange Commission. Accordingly, the unaudited condensed consolidated financial statements do not include all information and footnotes required by accounting principles generally accepted in the United States of America for complete annual financial statements. In the opinion of management, the accompanying unaudited condensed consolidated financial statements reflect all adjustments, consisting of only normal recurring adjustments, considered necessary for a fair presentation. Interim operating results are not necessarily indicative of results that may be expected for the year ending December 31, 2011 or for any other interim period. These unaudited condensed consolidated financial statements should be read in conjunction with the Company's audited financial statements as of and for the year ended December 31, 2010, which are included in the Company's Annual Report on Form 10-K for such year. The condensed balance sheet as of December 31, 2010 has been derived from the audited financial statements included in the Form 10-K for that year.

As of September 30, 2011, the Company has not generated any revenues from the development of its products and is therefore still considered to be a development stage company.

In March 2010, Manhattan entered into an Agreement and Plan of Merger (the "Merger Agreement") by and among the Company, Ariston Pharmaceuticals, Inc., a Delaware corporation ("Ariston") and Ariston Merger Corp., a Delaware corporation and wholly-owned subsidiary of the Company (the "Merger Sub"). Pursuant to the terms and conditions set forth in the Merger Agreement, the Merger Sub merged with and into Ariston (the "Merger"), with Ariston being the surviving corporation of the Merger. As a result of the Merger, Ariston became a wholly-owned subsidiary of Manhattan. The operating results of Ariston from March 8, 2010 to September 30, 2011 are included in the accompanying condensed consolidated statements of operations.

On June 20, 2011, the Company effected a 1 for 50 reverse stock split (the "Reverse Split"). All references to common shares and per share data for prior periods have been retroactively adjusted to reflect the Reverse Split as if it had occurred at the beginning of the earliest period presented.

On September 15, 2011, \$1,725,000 principal amount of 12% secured notes (See note 9) and interest thereon, amounting to \$676,072, converted into the right to receive 4,802,199 shares of the Company's common stock. These 4,802,199 issuable shares of the Company's common stock are reflected in these unaudited condensed consolidated financial statements as if the shares were issued on September 15, 2011. On September 15, 2011, the effective date of the conversion, the Company obtained from the holders of at least 2/3 of the original principal amount of the 12% secured notes their signed election to convert their 12% secured notes and interest into shares of the Company's common stock. The shares will be issued in the 4th quarter of 2011.

Segment Reporting

The Company has determined that it operates in only one segment currently, which is biopharmaceutical research and development.

## Financial Instruments

At December 31, 2010, the fair values of cash and cash equivalents, grant receivable, accounts payable, the convertible 5% notes payable, the ICON convertible note payable, the non-interest bearing note payable and the secured 12% notes payable approximate their carrying values. At September 30, 2011, the fair values of cash and cash equivalents, accounts payable, the convertible 5% notes payable, the ICON convertible note payable and the non-interest bearing note payable approximate their carrying values.

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### Investment in Joint Venture

The Company accounted for its investment in a joint venture using the equity method of accounting up through January 4, 2011, the date of the settlement agreement discussed in Note 6, and the cost method subsequent to January 4, 2011. Under the equity method, the Company records its pro-rata share of joint venture income or losses and adjusts the basis of its investment accordingly.

### Fair Value Measurements

The Company uses a standard framework in how to value the fair value of assets and liabilities. This framework is intended to increase consistency in how fair value determinations are made under various existing accounting standards that permit, or in some cases require, estimates of fair market value. This standard also expands financial statement disclosure requirements about a company's use of fair value measurements, including the effect of such measures on earnings.

This standard defines fair value as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. This standard also establishes a fair value hierarchy which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. That hierarchy is as follows:

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

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

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

The Company utilizes the market approach to measure fair value of its financial assets and liabilities. The market approach uses prices and other relevant information generated by market transactions involving identical or comparable assets and liabilities. The Company's financial assets (cash equivalents) as of September 30, 2011 and December 31, 2010 were held in money market funds which is a Level 1 measurable input.

The Company utilizes the Black-Scholes Option Pricing model to estimate the fair value of its derivative liabilities associated with warrant obligations and a convertible note obligation (see Note 10). The Company considers them to be Level 3 instruments. The following table shows the weighted average assumptions the Company used to develop the fair value estimates for the determination of the derivative liabilities at September 30, 2011 and 2010:

	September 30,	
	2011	2010
Fair value	\$ 0.052 - \$0.084	\$ 0.695 - \$0.835
Expected volatility	89 %	88 %
Dividend yield	-	-
Expected term (in years)	2.14 - 3.52	2.51 - 4.52
Risk-free interest rate	0.69 %	0.96 %



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The following table summarizes the changes in Level 3 instruments for the nine month periods ended September 30, 2011 and 2010:

	September 30,	
	2011	2010
Fair value at January 1	\$ 534,846	\$ 784,777
Purchases, sales, issuances and settlements	43,571	3,272,121
Net unrealized (gain)/loss	(39,587 )	(2,696,900)
Fair value at September 30	\$ 538,830	\$ 1,359,998

#### New Accounting Pronouncements

In April 2010, the FASB issued a new pronouncement “Revenue Recognition – Milestone Method”. This pronouncement provides guidance on the criteria that should be met for determining whether the milestone method of revenue recognition is appropriate. A vendor can recognize consideration that is contingent upon achievement of a milestone in its entirety as revenue in the period in which the milestone is achieved only if the milestone meets all criteria to be considered substantive. The following criteria must be met for a milestone to be considered substantive. The consideration earned by achieving the milestone should: 1. Be commensurate with either the level of effort required to achieve the milestone or the enhancement of the value of the item delivered as a result of a specific outcome resulting from the vendor’s performance to achieve the milestone; 2. Related solely to past performance; and 3. Be reasonably relative to all deliverables and payment terms in the arrangement. No bifurcation of an individual milestone is allowed and there can be more than one milestone in an arrangement. Accordingly, an arrangement may contain both substantive and non-substantive milestones. This pronouncement became effective on a prospective basis for milestones achieved in fiscal years beginning on or after June 15, 2010. The adoption of this guidance does not have a material impact on our financial statements.

## 2. LIQUIDITY

The Company had net income of \$298,105 and negative cash flows from operating activities of \$166,388 for the nine month period ended September 30, 2011. Net income for the nine month period ended September 30, 2011 includes a \$4,517,488 gain on settlement with Nordic Biotech Ventures II K/S of which \$4,017,488 was non cash and a loss on the early extinguishment of debt of \$1,225,912 as a result of the conversion of 12% secured notes and interest thereon (see Note 9). The net loss applicable to common shares from date of inception, August 6, 2001, to September 30, 2011 amounts to \$61,011,685.

During the nine months ended September 30, 2011 the Company received approximately \$0.5 million from the Nordic Settlement (see Note 6) and \$244,479 from a grant receivable, and repaid \$100,000 of principal on the ICON note payable (see Note 9).

During the nine months ended September 30, 2010 the Company received approximately \$2.2 million from an equity financing transaction (see Note 7) and approximately \$40,000 from Ariston Pharmaceuticals, Inc. in exchange for a note. In addition, approximately \$422,000 of notes payable and interest payable thereon was converted in this equity transaction. The Company repaid the \$40,000 received from Ariston in the first quarter of 2010 and the \$27,000 received from Ariston in the fourth quarter of 2009 together with interest thereon prior to the Merger.



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Management believes that the Company will continue to incur net losses through at least September 30, 2012 and for the foreseeable future. Based on the resources of the Company available at September 30, 2011, management believes that the Company has sufficient capital to fund its operations through the end of 2011. Management believes that the Company will need additional equity or debt financing or generate revenues through licensing of its products or entering into strategic alliances to be able to sustain its operations into 2012. Furthermore, the Company will need additional financing thereafter to complete development and commercialization of its products. There can be no assurances that we can successfully complete development and commercialization of our products. In addition, \$250,000 of debt matures in October 2011, the Company is currently negotiating an extension of the maturity of this debt, and \$1,725,000 principal amount of debt plus interest thereon that was to mature in December 2011 converted into equity during the quarter ended September 30, 2011 (see Note 9).

The Company's continued operation will depend on its ability to raise additional funds through various potential sources such as equity and debt financing, collaborative agreements, strategic alliances and its ability to realize the full potential of its technology in development. Additional funds may not become available on acceptable terms, and there can be no assurance that any additional funding that the Company does obtain will be sufficient to meet the Company's needs in the long-term.

These matters raise substantial doubt about the Company's ability to continue as a going concern. The accompanying financial statements do not include any adjustments that might result from the outcome of this uncertainty.

3. REVERSE STOCK SPLIT

The Company implemented a 1-for-50 reverse stock split of its common stock, \$0.001 par value per share on June 20, 2011 (the "Reverse Split"). The split-adjusted shares of the Company's Common Stock began trading on the OTCBB on July 14, 2011 under the symbol "MHAND," with a "D" added for 20 trading days to signify that the reverse stock split has occurred. A new CUSIP number has been assigned to the Company's Common Stock as a result of the reverse split.

The reverse Stock Split did not change the par value of the Company's Common Stock, which remains at \$0.001 per share, or the number of shares of common stock the Company is authorized to issue, which remains at 500,000,000 shares. At the Company's Annual Meeting of Stockholders held on May 20, 2011, the Company's stockholders approved a proposal authorizing the Company's Board of Directors (the "Board"), at its discretion, to amend the Company's Amended and Restated Certificate of Incorporation, as amended (the "Certificate of Incorporation"), to effect a reverse stock split of the Company's issued and outstanding shares of common stock, par value \$0.001 per share, within the range of 1-for-25 and 1-for-50, inclusive, without further approval or authorization of the Company's stockholders if the Board determines in the future that such a reverse stock split is in the best interests of the stockholders. This 1-for-50 reverse stock split was approved by the Company's Board of Director pursuant to such stockholder authorization.

Details of the Reverse Split:

- At June 20, 2011, immediately and without further action by the Company's stockholders, every fifty (50) shares of the Company's pre-split Common Stock, par value \$0.001 per share, was automatically converted into one (1) share of post-split Common Stock, par value \$0.001 per share. Accordingly, the Company's approximately 129.8 million pre-split shares of common stock outstanding will be combined into approximately 2.6 million post-split shares outstanding. The reverse stock split affects all issued and outstanding shares of the Company's Common Stock immediately prior to June 20, 2011. In addition, proportional adjustments will be made to the Company's equity

awards, outstanding warrants and convertible notes.

- Continental Stock Transfer and Trust Company, Manhattan's transfer agent, will act as exchange agent for the exchange. Stockholders will receive forms and notices to exchange their existing shares for new shares from the exchange agent or their broker. No fractional shares will be issued. Stockholders who otherwise would be entitled to receive fractional shares because they hold a number of shares not evenly divisible by 50, will automatically receive one whole share of Common Stock in lieu of the fractional share.



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As a result of the Reverse Split the 12% secured notes (see Note 9) and interest thereon became convertible, and did convert, into common stock at \$0.50 (\$0.01 on a pre-Reverse Split basis). This triggered the anti-dilution rights of certain warrant holders. All share amounts are reflected in these financial statements on a post-Reverse Split basis and reflect the conversion of the 12% secured notes and the anti-dilution rights. The following table illustrates the effects of the Reverse Split, the conversion of the 12% secured notes and the anti-dilution rights.

	Pre-Reverse Split	Anti-dilution Effect	Reverse Split Effect	Conversion of 12% Secured Notes and Interest	As of September 30, 2011, Post-Reverse Split, Anti-dilution and Conversion
<b>Shares outstanding:</b>					
Before conversion of 12% Secured Notes	129,793,289		(127,197,423 )		2,595,866
Conversion of 12% Secured Notes				4,802,199	4,802,199
After conversion	129,793,289	-	(127,197,423 )	4,802,199	7,398,065
<b>Shares issuable:</b>					
Warrants with antidilution rights	129,911,363	963,038,387	(1,071,090,755)		21,858,995
Warrants without antidilution rights	12,989,189		(12,729,405 )		259,784
Options	11,564,936		(11,333,637 )		231,299
Ariston milestone shares	15,890,452		(15,572,643 )		317,809
12% Secured Notes and interest	240,107,200		(235,305,001 )	(4,802,199 )	-
Other Convertible debt	45,776,620		(44,861,088 )		915,532
Total shares issued and issuable	586,033,049	963,038,387	(1,518,089,952)	-	30,981,484

#### 4. COMPUTATION OF NET INCOME (LOSS) PER COMMON SHARE

Basic net income (loss) per common share is calculated by dividing net income (loss) applicable to common shares by the weighted-average number of common shares outstanding for the period. Diluted net income (loss) per common share is the same as basic net income (loss) per common share for the three and nine month periods ended September 30, 2011 and 2010, since potentially dilutive securities would have an anti-dilutive effect either because such potentially dilutive securities were out of the money and the Company realized net income in the period or because the Company incurred a net loss in the period. The amounts of potentially dilutive securities excluded from the calculation were 23,265,610 and 4,231,197 shares at September 30, 2011 and 2010, respectively.

#### 5. SHARE-BASED COMPENSATION

The Company has stockholder-approved stock incentive plans for employees, directors, officers and consultants. Prior to January 1, 2006, the Company accounted for the employee, director and officer plans using the intrinsic value method. On January 1, 2006, the Company adopted the share-based payment method for employee options using the modified prospective transition method.

The Company recognizes compensation expense related to stock option grants on a straight-line basis over the vesting period. The Company recognized share-based compensation cost of \$19,210 and \$211,771 for the nine months

ended September 30, 2011 and 2010, respectively. The Company recognized share-based compensation cost of \$5,597 and \$5,630 for the three months ended September 20, 2011 and 2010, respectively. The Company did not capitalize any share-based compensation cost.

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Options granted to consultants and other non-employees are recorded at fair value at the date of grant and subsequently adjusted to fair value at the end of each reporting period until such options vest, and the fair value of the options, as adjusted, is amortized to consulting expense over the related vesting period. As a result of adjusting consultant and other non-employee options to fair value, the Company recognized share-based compensation cost of \$0 and \$107, respectively, for the three and nine month periods ended September 30, 2011 and 2010. The Company has allocated share-based compensation costs to general and administrative and research and development expenses as follows:

	Three months ended September 30,		Nine months ended September 30,	
	2011	2010	2011	2010
<b>General and administrative expense:</b>				
Share-based employee compensation cost	\$ 5,597	\$ 5,597	\$ 19,210	\$ 211,664
Share-based consultant and non-employee cost	-	3	-	11
Total general and administrative expense	5,597	5,600	19,210	211,675
<b>Research and development expense:</b>				
Share-based employee compensation cost	-	-	-	-
Share-based consultant and non-employee cost	-	30	-	96
Total research and development expense	-	30	-	96
<b>Total share-based cost</b>	<b>\$ 5,597</b>	<b>\$ 5,630</b>	<b>\$ 19,210</b>	<b>\$ 211,771</b>

To compute compensation charges in 2011 and 2010 the Company estimated the fair value of each option award on the date of grant using the Black-Scholes model. The Company based the expected volatility assumption on a volatility index of peer companies as the Company did not have a sufficient number of years of historical volatility of its common stock. The expected term of options granted represents the period of time that options are expected to be outstanding. The Company estimated the expected term of stock options by the simplified method. The expected forfeiture rates are based on the historical employee forfeiture experiences. To determine the risk-free interest rate, the Company utilized the U.S. Treasury yield curve in effect at the time of grant with a term consistent with the expected term of the Company's awards. The Company has not declared a dividend on its common stock since its inception and has no intentions of declaring a dividend in the foreseeable future and therefore used a dividend yield of zero.

The following table shows the weighted average assumptions the Company used to develop the fair value estimates for the stock options granted in the nine month period ended September 30, 2010 (there were no options granted in the nine month period ended September 30, 2011):

Nine months ended  
September 30,

	2011	2010	
Expected volatility	-	88	%
Dividend yield	-	-	
Expected term (in years)	-	5.7	
Risk-free interest rate	-	2.46	%

The Company has shareholder-approved incentive stock option plans for employees under which it has granted non-qualified and incentive stock options. In December 2003, the Company established the 2003 Stock Option Plan (the "2003 Plan"), which provided for the granting of up to 108,000 options to officers, directors, employees and consultants for the purchase of stock. Subsequently, the Company increased the number of shares of common stock reserved for issuance under the 2003 Plan by 192,000. At September 30, 2011, 300,000 shares were authorized for issuance. The options have a maximum term of 10 years and vest over a period determined by the Company's Board of Directors (generally 3 years) and are issued at an exercise price equal to or greater than the fair market value of the shares at the date of grant. The 2003 Plan expires on December 10, 2013 or when all options have been granted, whichever is sooner. At September 30, 2011 options to purchase 208,754 shares were outstanding, 556 shares of common stock were issued and there were 90,690 shares reserved for future grants under the 2003 Plan.

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In July 1995, the Company established the 1995 Stock Option Plan (the "1995 Plan"), which provided for the granting of options to purchase up to 2,600 shares of the Company's common stock to officers, directors, employees and consultants. The 1995 Plan was amended several times to increase the number of shares reserved for stock option grants. In June 2005, the 1995 Plan expired and no further options can be granted. At September 30, 2011 options to purchase 22,545 shares were outstanding and no shares were reserved for future stock option grants under the 1995 Plan.

A summary of the status of the Company's stock options as of September 30, 2011 and changes during the period then ended is presented below:

	Shares	Weighted average exercise price	Weighted Average Remaining Contractual Term (years)	Aggregate Intrinsic Value
Outstanding at December 31, 2010	231,499	\$ 24.37	6.72	
Granted	-			
Exercised	-			
Cancelled	(200 )	\$ 14.00		
Outstanding at September 30, 2011	231,299	\$ 24.37	5.19	\$ -
Exercisable at September 30, 2011	210,303	\$ 26.45	4.86	\$ -
Vested and expected to vest at September 30, 2011	229,404	\$ 24.54	5.16	\$ -

As of September 30, 2011, the total compensation cost related to nonvested option awards not yet recognized is \$36,904. The weighted average period over which it is expected to be recognized is approximately 1.43 years.

## 6. JOINT VENTURE

In February 2008, the Company and Nordic Biotech Advisors ApS through its investment fund Nordic Biotech Venture Fund II K/S ("Nordic") entered into a joint venture agreement (the "Hedrin JV Agreement") to develop and commercialize the Company's North American rights (under license) to its Hedrin product.

Pursuant to the Hedrin JV Agreement, Nordic formed a new Danish limited partnership, H Pharmaceuticals K/S, (the "Hedrin JV") and provided it with \$5.5 million funding in several tranches through January of 2010 and the Company assigned and transferred its North American rights in Hedrin to the Hedrin JV in return for a \$3.5 million cash payment from the Hedrin JV, paid in several tranches, and equity in the Hedrin JV representing 47.62% of the nominal equity interests in the Hedrin JV. Through January 2010 the Company recognized an investment in the Hedrin JV of \$0.75 million and an exchange obligation of \$3.95 million. The exchange obligation represents the Company's obligation to Nordic to issue the Company's common stock in exchange for all or a portion of Nordic's equity interest in the Hedrin JV upon the exercise by Nordic of the put issued to Nordic in the Hedrin JV Agreement transaction. The put is described below.

Nordic had an option to put all or a portion of its equity interest in the Hedrin JV to the Company in exchange for the Company's common stock (the "Nordic Put"). The Company had an option to, under certain conditions, call all or a portion of Nordic's equity interest in the Hedrin JV in exchange for the Company's common stock (the "Nordic Call"). The Nordic Put and the Nordic Call terminated upon the execution, on January 4, 2011, of a settlement and release agreement between Nordic and the Company. The settlement and release agreement is discussed below.

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Nordic paid the Company a non-refundable fee of \$150,000 in February 2008 for the right to receive a warrant covering shares of the Company's common stock. The warrant (the "Nordic Warrant") was issued in 2008. The Nordic Warrant terminated upon the execution, on January 4, 2011, of a settlement and release agreement between Nordic and the Company. The settlement and release agreement is discussed below.

The Hedrin JV is responsible for the development and commercialization of Hedrin for the North American market and all associated costs including clinical trials, regulatory costs, patent costs, and future milestone payments owed to Thornton & Ross, Ltd., the licensor of Hedrin.

The Hedrin JV engaged the Company to provide management services to the Hedrin JV in exchange for a management fee. For the nine months ended September 30, 2011 and 2010, the Company has recognized \$0 and \$225,000, respectively, of management fees earned from the Hedrin JV which is included in the Company's consolidated statements of operations as a component of interest and other income. The management services agreement terminated upon the execution, on January 4, 2011, of a settlement and release agreement between Nordic and the Company. The settlement and release agreement is discussed below.

As previously reported, the Company and Nordic have had various disputes relating to the Hedrin JV, to the Nordic Put and the Nordic Warrant. On January 4, 2011 the Company entered into a settlement and release agreement (the "Nordic Settlement") with Nordic and the Hedrin JV that resolves all disputes between and among the Company, Nordic and the Hedrin JV.

The principal terms of the Nordic Settlement are:

- The Nordic Put has been terminated. The Company believed the Nordic Put permitted Nordic to become the owner, upon exercise of the Nordic Put, of 1,428,571 shares of the Company's common stock. Nordic asserted that the Nordic Put would have permitted Nordic to become the owner of 3,666,666 shares of the Company's common stock.
- The Nordic Warrant has been terminated. The Company believed the Nordic Warrant covered 285,714 shares of the Company's common stock. Nordic asserted that the Nordic Warrant covered 666,666 shares of the Company's common stock.
- Nordic was required to make an additional, non-dilutive capital contribution to the Hedrin JV of \$1,500,000, which includes \$300,000 contributed to the Hedrin JV by Nordic on December 15, 2010.
- The Hedrin JV has paid to the Company a settlement amount of \$500,000, less any "Excess Payment" (defined below). An "Excess Payment" is the amount by which Nordic's and the Hedrin JV's reasonable out-of-pocket legal and other costs incurred with respect to the Settlement and Release Agreement exceed \$70,000. To date there have been no Excess Payments.
- Our equity interest in the Hedrin JV was reduced to 15%, and further reductions in our equity interest are possible if and when Nordic makes additional capital contributions to the Hedrin JV. In no event shall the capital contributions by Nordic reduce our ownership in the Hedrin JV below 5%.
- The Hedrin JV has paid \$75,000 to the Company under the Services Agreement, dated February 21, 2008, and that Services Agreement is terminated as of December 31, 2010.
- The Hedrin JV Agreement, dated January 31, 2008, as amended on February 18, 2008, and as further amended by an Omnibus Amendment on June 9, 2008, between the Company and Nordic; the Shareholders' Agreement, dated February 21, 2008, as amended by an Omnibus Amendment on June 9, 2008, with respect to the Hedrin JV, and the Registration Rights Agreement, dated February 25, 2009, are terminated.





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At December 31, 2010 the Company had unrecognized equity in its share of the losses of the Hedrin JV of approximately \$560,000. In conjunction with the Nordic Settlement the Company recognized this \$560,000 of its share of the losses of the Hedrin JV during the nine months ended September 30, 2011. The Company also recognized a gain on the Nordic Settlement of approximately \$4.5 million during the nine months ended September 30, 2011. The components of the gain on the Nordic Settlement are as follows:

	Total	Cash portion	Non cash portion
Exchange obligation, termination of the Nordic Put	\$ 3,949,176	\$ -	\$ 3,949,176
Termination of the Nordic Warrant	71,429	-	71,429
Payment of settlement amount	500,000	500,000	-
Other	(3,117 )	-	(3,117 )
Totals	\$ 4,517,488	\$ 500,000	\$ 4,017,488

On April 19, 2011 H Pharmaceuticals K/S (the "Hedrin JV"), of which the Company was a 15% limited partner at the time, filed a demand for arbitration against Thornton & Ross, LTD. ("T&R") with respect to alleged breaches by T&R of an Exclusive License Agreement (the "Hedrin License") dated June 28, 2007, which was originally entered into between the Company and T&R, and which the Company assigned in 2008 to the Hedrin JV, with T&R's consent. The Hedrin JV is seeking damages from T&R in the amount of approximately \$7,000,000. The Company was not a party to the initial arbitration demand.

On May 20, 2011 T&R filed an answer to the arbitration demand in which T&R asserted counterclaims against the Hedrin JV for alleged breaches by the Hedrin JV of the Hedrin License and for declaratory relief that the Hedrin License was properly terminated by T&R. In addition, T&R has impleaded an individual (who is not associated with the Company), Nordic Biotech Venture Fund II K/S (an investment fund) and the Company, demanding arbitration against them based on alleged breaches of the Hedrin License and other related claims. T&R is seeking damages of approximately \$20,000,000.

The Company has not yet responded to the arbitration demand against it, but believes that T&R's claims against the Company are without merit. The arbitration has begun between the Hedrin JV and T&R without the Company being named as a participant. The Hedrin JV and T&R held a mediation session in order to avoid the arbitration process. The mediation process did not produce a result. Nordic has recently made an additional capital contribution to the Hedrin JV in order to fund the arbitration. As a result of that capital contribution the Company now owns an 11% interest in the Hedrin JV.

## 7. 2010 EQUITY FINANCING

On March 2, 2010, the Company raised aggregate gross proceeds of approximately \$2,547,500 pursuant to a private placement of its securities (the "2010 Equity Financing"). The Company entered into subscription agreements (the "Subscription Agreements") with seventy-seven accredited investors (the "Investors") pursuant to which the Company sold an aggregate of 101.9 Units (as defined herein) for a purchase price of \$25,000 per Unit. Pursuant to the Subscription Agreements, the Company issued to each Investor units (the "Units") consisting of (i) 7,143 shares of common stock, \$0.001 par value per share (the "Common Stock" or "Shares") of the Company and (ii) 10,714 warrants (each a "Warrant" and collectively the "Warrants"), each of which will entitle the holder to purchase one additional share

of Common Stock for a period of five years (each a “Warrant Share” and collectively the “Warrant Shares”) at an exercise price of \$0.08 per share. Because the Warrant Shares are convertible into shares of the Company, subject to adjustment, the conversion feature is subject to Derivative Liability accounting (see Note 10).

National Securities Corporation (“National”) was the placement agent for the 2010 Equity Financing transaction. In connection with the issuance of the Securities, the Company issued warrants to purchase an aggregate of 72,786 shares of Common Stock at an exercise price of \$4.00 per share, subject to adjustment, to the placement agent and certain of its designees. Because the warrant is convertible into shares of the Company, subject to adjustment, the warrants are subject to Derivative Liability accounting (see Note 10). The warrants expire on March 2, 2015.

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All of the Investors represented that they were “accredited investors,” as that term is defined in Rule 501(a) of Regulation D under the Securities Act, and the sale of the Units was made in reliance on exemptions provided by Regulation D and Section 4(2) of the Securities Act of 1933, as amended.

In connection with the closing of the private placement, the Company, the placement agent acting in connection with the private placement (the “Placement Agent”) and the Investors entered into a Registration Rights Agreement, dated as of March 2, 2010, and the Company agreed to, and did, file a registration statement to register the resale of the Shares, within 60 days of the final closing date and the registration statement was declared effective within the time limits of the Registration Rights Agreement.

The Company received net proceeds of approximately \$2,100,000 after payment of an aggregate of approximately \$300,000 of commissions and expense allowance to the Placement Agent, and approximately \$100,000 of other offering and related costs in connection with the private placement.

The Company did not use any form of advertising or general solicitation in connection with the sale of the Units. The Shares, the Warrants and the Warrant Shares are non-transferable in the absence of an effective registration statement under the Act, or an available exemption there from, and all certificates are imprinted with a restrictive legend to that effect.

On April 8, 2010, the Company completed the final closing of the 2010 Equity Financing. In connection with the final closing, the Company sold an aggregate of 2.4 additional Units and received net proceeds of approximately \$51,700 after payment of an aggregate of \$8,300 of commissions and expense allowance to placement agent. In connection with the final closing, the Company also issued a warrant to purchase 257 shares of Common Stock at an exercise price of \$4.00 per share to the placement agent as additional compensation for its services.

In addition, on April 8, 2010, the holder of the Convertible 12% Note (see Note 8) with a stated value of \$400,000 and \$22,000 of accrued interest, exercised its option to convert its Debenture (including all accrued interest thereon) into 16.88 Units. The conversion price was equal to the per Unit purchase price paid by the Investors in the private placement.

The Company issued a total of 137,714 shares of Common Stock and Warrants to purchase 206,571 shares of Common Stock at an exercise price of \$4.00 per share to the investors in the final closing of the 2010 Equity Financing, including the conversion of the 12% Convertible Note.

#### 8. ARISTON MERGER

On March 8, 2010, the Company entered into the Merger Agreement by and among the Company, Ariston and Merger Sub. Pursuant to the terms and conditions set forth in the Merger Agreement, on March 8, 2010, the Merger Sub merged with and into Ariston, with Ariston being the surviving corporation of the Merger. As a result of the Merger, Ariston became a wholly-owned subsidiary of the Company.

Under the terms of the Merger Agreement, the consideration payable by Manhattan to the stockholders and note holders of Ariston consists of the issuance of 1,412,488 shares of Manhattan’s common stock, par value \$0.001 per share, (“Common Stock”) at Closing (as defined in the Merger Agreement) plus the right to receive up to an additional 494,370 shares of Common Stock (the “Milestone Shares”) upon the achievement of certain product-related milestones

described below. In addition, Manhattan has reserved 772,624 shares of its Common Stock for possible future issuance in connection with the conversion of \$15.45 million of outstanding Ariston convertible promissory notes. The noteholders will not have any recourse to Manhattan for repayment of the notes (their sole recourse being to Ariston), but the noteholders will have the right to convert the notes into shares of the Manhattan's Common Stock at the rate of \$20.00 per share. Further, Manhattan has reserved 100,000 shares of its Common Stock for possible future issuance in connection with the conversion of the \$1.0 million outstanding Ariston convertible promissory note issued in satisfaction of a trade payable. The noteholder will not have any recourse to Manhattan for repayment of the note (their sole recourse being to Ariston), but the noteholder will have the right to convert the note into shares of Manhattan's Common Stock at the rate of \$10.00 per share.

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Upon the achievement of the milestones described below, Manhattan would be obligated to issue portions of the Milestone Shares to the former Ariston stockholders and noteholders:

- Upon the affirmative decision of Manhattan’s Board of Directors, provided that such decision is made prior to March 8, 2011, to further develop the AST-915, either internally or through a corporate partnership, Manhattan would issue 176,561 of the Milestone Shares. This milestone was attained in January 2011 and the shares were issued in March 2011. The Company recognized approximately \$220,000 of research and development expense during the nine months ended September 30, 2011 from the issuance of these shares.
- Upon the acceptance by the FDA of the Ariston’s filing of the first New Drug Application for the AST-726 product candidate, Manhattan would issue 141,248 of the Milestone Shares.
- Upon the Company receiving FDA approval to market the AST-726 product candidate in the United States of America, Manhattan would issue 176,561 of the Milestone Shares.

Certain members and former members of Manhattan’s board of directors and principal stockholders of Manhattan at the time of the Merger owned Ariston securities as of the closing of the Merger:

- Timothy McInerney, a former director of Manhattan, owned 333 shares of Ariston common stock which represented less than 1% of Ariston’s outstanding common stock as of the closing of the Merger.
- Neil Herskowitz, a director of Manhattan, indirectly owned convertible promissory notes of Ariston with interest and principal in the amount of \$192,739.
- Michael Weiser, a former director of Manhattan, owned 2,347 shares of Ariston common stock, which represented approximately 2.1% of Ariston’s outstanding common stock as of the closing of the Merger.
- Lindsay Rosenwald, a more than 5% beneficial owner of Manhattan common stock, in his individual capacity and indirectly through trusts and companies he controls, owned 9,958 shares of Ariston common stock, which represented approximately 8.9% of Ariston’s outstanding common stock as of the closing of the Merger and indirectly owned convertible promissory notes of Ariston in the amount of \$141,438.

The Company merged with Ariston principally to add new products to its portfolio. Prior to the Merger, Ariston was a private, clinical stage specialty biopharmaceutical company based in Shrewsbury, Massachusetts that in-licensed, developed and planned to market novel therapeutics for the treatment of serious disorders of the central and peripheral nervous systems.

The Merger date fair value of the total consideration paid was \$1,491,937 which consisted of 141,248 shares of the Company’s common stock issued upon the Merger and 317,809 contingently issuable shares upon Ariston’s attaining certain milestones as described above. At the time of the Merger, the Company did not believe the attainment of the milestone for AST-915 was highly probable and, therefore, recorded no contingent consideration relative to it. The par value of the contingently issuable common shares is reflected in the accompanying consolidated balance sheets as of September 30, 2011 and December 31, 2010 as a component of stockholders’ deficiency, contingently issuable shares. The Company incurred \$9,527 of acquisition related costs.

The following table summarizes the fair values of the assets acquired and liabilities assumed at the Merger date:

Cash and cash equivalents	\$ 519,365
Other assets	120,870
<b>Total identifiable assets</b>	<b>640,235</b>

Accounts payable and accrued expenses	437,615
ICON convertible note payable	1,000,000
5% convertible notes payable	15,452,793
Total identifiable liabilities	16,890,408
Net identifiable assets (liabilities)	(16,250,173)
In-process research and development acquired	17,742,110
Net assets acquired	\$1,491,937

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The following supplemental pro forma information presents the financial results as if the acquisition of Ariston had occurred on January 1, 2010 for the three and nine month periods ended September 30, 2010. This supplemental pro forma information has been prepared for comparative purposes and does not purport to be indicative of what would have occurred had the acquisition been made on January 1, 2010, nor are they indicative of future results.

	Three Month Period Ended September 30, 2010	Nine Month Period Ended September 30, 2010
Pro forma consolidated results:		
Revenue	\$ -	\$ -
Net income	\$ 41,247	\$ 104,411
Basic and diluted income per share	\$ 0.02	\$ 0.05

#### 9. NOTES PAYABLE

The following is a summary of Notes Payable:

	At September 30, 2011			At December 31, 2010		
	Current portion, net	Non-current portion, net	Total	Current portion, net	Non-current portion, net	Total
Secured 12% Note Payable, Net	\$-	\$-	\$-	\$1,722,346	\$-	\$1,722,346
Non-interest Bearing Note Payable, Net	246,900	-	246,900	231,900	-	231,900
Convertible 5% Notes Payable	-	16,225,433	16,225,433	-	15,452,793	15,452,793
ICON Convertible Note	514,414	163,364	677,778	100,000	677,778	777,778
<b>Total</b>	<b>\$761,314</b>	<b>\$16,388,797</b>	<b>\$17,150,111</b>	<b>\$2,054,246</b>	<b>\$16,130,571</b>	<b>\$18,184,817</b>

##### a. Secured 12% Notes Payable

In 2008 and 2009 the Company sold \$1,725,000 of 12% senior secured notes (the "Secured 12% Notes") that mature two years after issuance and issued warrants to the investors to purchase 1.15 million shares of the Company's common stock at \$4.50 per share. The warrants expire on December 31, 2013. Net proceeds of \$1.4 million were realized and \$78,000 of issuance costs were paid outside of the closings.

On February 9, 2011, the Company entered into a waiver and forbearance agreement (the "Extension Agreement") with the requisite holders of the Secured 12% Notes whereby the holders of the notes (the "Noteholders") agreed to forbear the exercise of their rights under the Notes and waive the default thereof until December 31, 2011. As part of the Extension Agreement, the Company has agreed to take and has taken prompt steps to seek to reduce its outstanding indebtedness by permitting the Noteholders to convert the Secured 12% Notes into shares of the Company's common stock at a conversion price of \$0.50 per share and to amend the terms of the warrants issued with the Secured 12% Notes to include a full-ratchet anti-dilution feature and an exercise price of \$0.50 per share. The Company obtained

stockholder approval to, among other things, increase the number of its authorized common stock. The Company has increased its authorized shares of common stock through the Reverse Split. As a result of the Reverse Split the Secured 12% Notes became convertible into common stock at a conversion price of \$0.50, this triggered the antidilution rights of the warrants issued with Secured 12% Notes, the warrants issued with the Convertible 12% Note and the warrants issued in the 2010 Equity Pipe. The Secured 12% Notes and interest thereon, amounting to \$676,072 at the time of conversion, converted into the right to receive 4,802,199 shares of the Company's common stock on September 15, 2011 (the "Secured Debt Conversion").



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National Securities Corporation (“National”) was the placement agent for the Secured 12% Notes Transaction. The Company issued to National, as a component of their placement agent fee, Warrants to purchase 0.2 million shares of the Company’s common stock at \$4.50 per share. The Warrants expire on December 31, 2013.

Interest on the Secured 12% Notes is compounded quarterly and was payable at maturity. At December 31, 2010, accrued and unpaid interest on the Secured 12% Notes amounted to approximately \$481,000, and is reflected in the accompanying balance sheet December 31, 2010 as part of interest payable. The Secured 12% Notes are secured by a pledge of all of the Company’s assets except for its investment in the Hedrin JV. In addition, to provide additional security for the Company’s obligations under the notes, the Company entered into a default agreement, which provides that upon an event of default under the notes, the Company shall, at the request of the holders of the notes, use reasonable commercial efforts to either (i) sell a part or all of the Company’s interests in the Hedrin joint venture or (ii) transfer all or part of the Company’s interest in the Hedrin JV to the holders of the notes, as necessary, in order to fulfill the Company’s obligations under the notes, to the extent required and to the extent permitted by the applicable Hedrin joint venture agreements.

The Company incurred a total of approximately \$424,000 of costs in the issuance of the \$1,725,000 of Secured 12% Notes sold in 2008 and 2009. These costs were capitalized and were amortized over the life of the Secured 12% Notes into interest expense. During the nine months ended September 30, 2011 and the year ended December 31, 2010, the amount amortized into interest expense was approximately \$4,000 and \$197,000, respectively. At June 30, 2011 the costs of issuance were fully amortized. At December 31, 2010 the remaining unamortized balance of approximately \$4,000 is reflected in the accompanying balance sheet as of December 31, 2010 as debt issue costs.

The Company recognized an original issue discount (the “OID”) of approximately \$194,000 on the issuance of the Secured 12% Notes sold for the value of the warrants issued to the investors. The OID was being amortized over the life of the Secured 12% Notes into interest expense. During the nine months ended September 30, 2011 and year ended December 31, 2010 the amount amortized into interest expense was approximately \$3,000 and \$91,000, respectively. At June 30, 2011 the OID was fully amortized. At December 31, 2010 the remaining unamortized balance of approximately \$3,000 has been netted against the face amount of Notes Payable in the accompanying balance sheet as of December 31, 2010.

The closing market price of the Company’s common stock on February 9, 2011 was greater than the conversion price, therefore the Company recognized a beneficial conversion feature of \$1,725,000 on the Secured 12% Notes and \$502,949 on interest payable on the Secured 12% Notes. The closing market price of the Company’s common stock on March 31, 2011 was greater than the conversion price, therefore the Company recognized an additional beneficial conversion feature of \$17,647 on interest payable on the Secured 12% Notes. The closing market price of the Company’s common stock on June 30, 2011 was less than the conversion price, therefore there was no beneficial conversion charges for the interest during the quarter ended June 30, 2011. The beneficial conversion feature has been recorded as a discount on the Secured 12% Notes and on the interest payable on the Secured 12% Notes. The Secured 12% Notes became convertible upon the execution of the Reverse Split on June 20, 2011. The beneficial conversion feature was amortized on a straight-line basis over the remaining term of the Secured 12% Notes (June 20, 2011 through December 31, 2011). The Company amortized \$1,019,684 of the beneficial conversion feature for the nine months ended September 30, 2011, which is reflected in the accompanying Statement of Operations as a component of interest expense. At the date of the Secured Debt Conversion the unamortized portion of the beneficial conversion feature amounted to \$1,225,912 and was charged to income as loss on early extinguishment of debt.

b. 8% Note Payable

On December 21, 2009, the Company entered into a Future Advance Promissory Note (the "8% Note") with Ariston under which the Company may withdraw up to \$67,000 bearing interest at a rate of 8%. As of December 31, 2009, the Company had withdrawn \$27,000 from Ariston subject to the terms of the 8% Note. On January 13, 2010, the Company withdrew an additional \$20,000 subject to the 8% Note and on January 28, 2010, the Company withdrew an additional \$20,000 subject to the 8% Note. On March 4, 2010, the Company repaid Ariston the \$67,000 withdrawn subject to the 8% Note and accrued interest of \$816.

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c. Non-interest Bearing Note Payable

On October 27, 2009, the Company entered into a Settlement Agreement and Mutual Release with Swiss Pharma Contract LTD (“Swiss Pharma”) pursuant to which the Company agreed to pay Swiss Pharma \$200,000 and issue to Swiss Pharma an interest free promissory note due on October 27, 2011 in the principal amount of \$250,000 in full satisfaction of the September 5, 2008 arbitration award.

In connection with the non-interest bearing note, the Company recognized an original issue discount of \$40,000 of imputed interest on the note, which is being amortized into interest expense on a straight-line basis over the two-year term of the note. For the nine months ended September 30, 2011 and the year ended December 31, 2010, the Company amortized \$15,000 and \$20,000 of the OID into interest expense, respectively. The remaining unamortized balances of \$3,100 and \$18,100 have been netted against the face amount of Notes payable, current portion, net in the accompanying balance sheets as of September 30, 2011 and December 31, 2010, respectively.

d. Convertible 12% Note Payable

In October 2009, the Company sold a 12% Original Issue Discount Senior Subordinated Convertible Debenture with a stated value of \$400,000 (the “Convertible 12% Note”) and a warrant to purchase 44,444 shares of the Company’s common stock for a purchase price of \$200,000. National was the placement agent for the Convertible 12% Note transaction. The Company issued to National, as a component of their placement agent fee, warrants to purchase 4,444 shares of the Company’s common stock. The warrants issued to the investors and National expire in October 2014 and were exercisable at an original price of \$5.50 per share, subject to adjustment. As a result of the 2010 Equity Financing the exercise price and number of shares represented by these warrants adjusted to 69,841 shares at \$3.50 per share for the investors and 6,984 shares at \$3.50 per share for National.

The Convertible 12% Note was convertible into shares of the Company’s common stock in the event the Company issues new securities in connection with a financing. The Convertible 12% Note may be converted into such new securities at a conversion price equal to the purchase price paid by the purchasers of such new securities. On April 8, 2010, the holder of the Convertible 12% Note exercised its option to convert its note, including all accrued interest thereon, into 16.88 Units of the 2010 Equity Financing.

e. Convertible 5% Notes Payable

Upon the Merger, Ariston issued \$15,452,793 of five-year 5% notes payable (the “5% Notes”) in satisfaction of several note payable issuances. The cumulative liability including accrued and unpaid interest of these several issuances of notes was \$15,452,793 as of the Merger date. The 5% Notes and accrued and unpaid interest thereon are convertible at the option of the holder into the Manhattan’s common stock at the conversion price of \$20 per share. Ariston agreed to make quarterly payments on the 5% Notes equal to 50% of the net product cash flow received from the exploitation or commercialization of Ariston’s product candidates, AST-726 and AST-915. The 5% Notes are solely the obligation of Ariston and have no recourse to Manhattan other than the conversion feature discussed above. Interest accrues monthly, is added to principal on an annual basis, every March 8, and is payable at maturity. For the nine months ended September 30, 2011, the Company recorded approximately \$601,000 of interest expense on the 5% Notes. On March 8, 2011 the accrued and unpaid interest on the 5% Notes was \$772,640 and was added to the principal amount of the 5% Notes Payable. At September 30, 2011 the principal amount of the 5% Notes was \$16,225,433 and interest payable on the 5% Notes Payable was \$455,214 and were reflected as components of notes payable, noncurrent portion, net and interest payable, noncurrent portion, respectively, in the accompanying balance sheet as of September 30, 2011. At December 31, 2010 the principal amount of the 5% Notes was \$15,452,793 and interest payable on the 5% Notes Payable was \$626,697 and were reflected as components of notes payable, noncurrent portion, net and

interest payable, noncurrent portion, respectively, in the accompanying balance sheet as of December 31, 2010.

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